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ENFORCEMENT OF THE EXPORT CONTROL ENFORCEMENT ACT

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

SECOND SESSION

TO CLARIFY ENFORCEMENT JURISDICTION OF THE EXPORT ADMINISTRATION ACT OF 1979, PARTICULARLY THE ASSIGNMENT OF THAT ENFORCEMENT ROLE TO THE AGENCY ABLE AND WILLING TO ENFORCE OUR EXPORT CONTROL LAWS AS REQUIRED BY THE CONGRESS AND CONSISTENT WITH OUR NATIONAL SECURITY AND FOREIGN POLICY NEEDS, IN LIGHT OF THE RECENT CASE INVOLVING THE ATTEMPTED TRANSFER OF A VAX 11/782 COMPUTER AND 50 TONS OF SENSITIVE GOODS AND TECHNOLOGY TO THE SOVIET UNION

APRIL 2, 1984

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Committee on Banking, Housing, and Urban Affairs

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ENFORCEMENT OF THE EXPORT CONTROL ENFORCEMENT ACT

MONDAY, APRIL 2, 1984

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, D.C.

The committee met at 10 a.m., in room SD-538, Dirksen Senate Office Building, Jake Garn (chairman of the committee) presiding.

Present: Senators Garn, Hecht, and Proxmire.

OPENING STATEMENT OF CHAIRMAN GARN

The CHAIRMAN. The Banking Committee will come to order.

This morning the Banking Committee will examine the enforcement of the Export Administration Act in light of the recent diversion case involving approximately 50 tons of sensitive goods and technology being smuggled to the Soviet Union, and in light of the recent policy of the administration regarding the conduct of foreign investigations.

This review is becoming an annual exercise. Unfortunately, the problems persist and we continually are found examining serious instances where our control effort has failed. We were told first that there was no enforcement problem. Then we were told that the Commerce Department was beefing up its efforts to put an end to the problem. Only with the help of the Customs Service, acting on a tip, were we able to uncover the largest diversion case in history, and stop the shipment—and only half of the shipment—at the last minute, even though the company diverting the controlled goods and technology had been under Commerce suspicion since 1981.

The recent case involving the attempted diversion to the Soviet Union of a sophisticated VAX 11/782 computer and 50 tons of additional high-tech equipment may shed some light on the reasons for the continuing problems in the enforcement of export controls. The Senate recently passed legislation that would transfer that enforcement responsibility to the Customs Service, our antismuggling, law enforcement agency.

This step is essential for an effective enforcement program. It will put an end to the existing competition between agencies over an area that is vital to our national security and foreign policy. Competition is healthy and necessary for business, but it is disruptive and dangerous in law enforcement. It is also disruptive in our efforts to obtain international cooperation when our allies witness our enforcement agencies tripping over one another in the conduct

of foreign investigations. Foreign governments are likely to become confused over whom they are to deal with, and established procedures for multilateral cooperation are violated.

Giving enforcement responsibilities to the Customs Service, as the Senate has chosen to do, is also prudent from a budgetary standpoint, since any enhancement of the Commerce Department's enforcement resources would be a duplication of customs facilities that are already in place. Moreover, for some reason, the Customs Service seems to work more quickly. Within hours of being tipped off about the potential VAX computer shipment to the Soviet Union the Customs Service had agents in the field making arrangements to intercept the shipment. Meanwhile, the Commerce Department had the companies responsible for diversion under investigation for several months without taking appropriate action. In fact, the Commerce Department resisted sharing essential information with the Customs Service once Customs began their enforcement effort.

In short, the recent decision by the administration to continue the status quo in enforcement of export controls is unacceptable. The status quo is endangering our national security. The only solution is to clarify enforcement jurisdiction in the law and give enforcement to the agency able and willing to enforce our export control laws as required by the Congress and consistent with our national security and foreign policy needs. That is not just my belief. That is not just the position I have pushed for the last several years. It has been expressed overwhelmingly by the entire Senate.

Senator Proxmire.

OPENING STATEMENT OF SENATOR PROXMIRE

Senator PROXMIRE. Thank you, Mr. Chairman.

Mr. Chairman, I certainly endorse everything you said in your statement. I would add that the VAX episode reveals the nature of the massive, well-managed, steal-the-American technology program being run by the Soviet Union. The Soviets are using our technology to build their military capabilities in microelectronics, lasers, radar, precision manufacturing, and other areas. The computer seized in this case would have allowed the Soviets to increase the accuracy and destructive force of their weaponry. Soviet leaders have made their steal American technology program a primary task of the Soviet intelligence services. The episode that is the subject of our hearing today is only the tip of the iceberg. It illustrates the disarray in our export control program, in the face of the Soviet challenge.

I am appalled by the advantage the Soviets are accruing by acquiring our expensively developed technology. It is absolutely clear that the weakness of our export control policy affects both our national security and our budget. American taxpayers are in effect paying for the Soviets to modernize their military machine. We cannot afford to continue policies that make this possible, particularly when defense budget requests are nearing $300 billion annually, and we are running a $200 billion budget deficit.

I don't mind spending money needed to safeguard our Nation's security, but I will not quietly accept a situation in which we spend

tens of billions to develop critical technologies, and then through feeble export controls allow the Soviets to obtain these technologies for next to nothing.

One big problem we have identified in our export control program is the bureaucratic bickering between our export control agencies. The Commerce Department, the Defense Department, and the Customs Service each have a role in administering our export control program. Each wants to guard its own turf. Commerce, which is our export promotion agency, has a built-in conflict of interest in administering export controls. It wants to limit the right of the Defense Department to review export licenses in the fear that Defense might interfere with export promotion. Commerce also fights the efforts of the Customs Service to help enforce our export control laws. It fears Customs will be too aggressive and hinder exporters of high-technology goods.

Recent efforts by the administration to paper over these interagency differences through memorandums of understanding [MOU] between these agencies are not satisfactory. They can be revoked at any time and since they don't have the force of law can be evaded by people in our export control agencies. If the administration were really serious about resolving the problems in our export control program, it would support the Banking Committee's Heinz/Garn amendments to the Export Administration Act. These amendments will strengthen our control program as follows:

One, by raising the priority and visibility of the export licensing program in the Commerce Department—so people dealing with controls are not under those whose principal interest is export promotion.

Two, by giving the Defense Department authority to review exports to any country where there is a clear risk of diversion to proscribed destinations.

Three, by transferring primary enforcement responsibilities from the Commerce Department to the Customs Service.

Four, by pressing our allies to work with us to control the export of critical technologies to the Soviets.

I urge our witnesses to put on the record their true views on the Senate bill and not be silenced by the administration's efforts to insure that they each toe the line in support of the administration's papering over of interagency differences.

The CHAIRMAN. Senator Hecht.

Senator HECHT. Thank you, Mr. Chairman. No statement.

The CHAIRMAN. Gentlemen, before you testify, could I have you stand and be sworn.

[Whereby, the witnesses were duly sworn.]

The CHAIRMAN. Gentlemen, we are pleased to have you with us today. This is a difficult subject, I realize. We have already conducted one closed hearing on this issue before the Banking Committee and this is an open hearing so obviously we have to avoid any classified information. I would caution you to do so. And we will as well. If as a result of this open hearing there is additional information that you wish to impart to the committee that is of a classified nature, we can certainly hold an additional closed hearing.

Mr. Archey, would you like to begin?

STATEMENT OF WILLIAM T. ARCHEY, ACTING ASSISTANT SECRETARY FOR TRADE ADMINISTRATION, DEPARTMENT OF COMMERCE

Mr. ARCHEY. Thank you, Senator. In response to your letter inviting me to testify there were three basic issues that were referenced. One is the state of cooperation in light of the President's recent decision between the Customs Service and the Commerce Department. No. 2 would be the focus in particular on the recent technology transfer case regarding South Africa. And the third, the improvements in the enforcement operations begun by the Commerce Department in the last few years.

I would like to just summarize my detailed statement and provide the entire statement for the record.

The CHAIRMAN. All of your statements will be placed in the record in full.

Mr. ARCHEY. Thank you, Mr. Chairman.

MEMORANDUM OF UNDERSTANDING ON THE EXPORT ADMINISTRATION ACT

As the committee is aware, on January 16, 1984, Lionel Olmer, Under Secretary of Commerce for International Trade, and John Walker, Assistant Secretary of Treasury for Enforcement and Operations, signed an MOU relating to the conduct of the Export Administration Act [EAA] investigations overseas. Two weeks ago, the President personally endorsed the MOU, and further concluded that Customs and Commerce bring important complementary assets to the enforcement of the EAA.

The MOU primarily deals with the overseas aspects of EAA investigations. The MOU provides that both Commerce—through its Office of Export Enforcement—and Treasury—through the U.S. Customs Service—will continue to conduct their own investigations overseas. The MOU clarifies who will initiate the contact abroad with foreign enforcement agencies. This liaison function will be the responsibility of the Customs Service in most countries. However, in those countries where the host government has established the export control enforcement function in a trade department, Commerce will provide its own liaison.

Those countries are Sweden, Belgium, Austria, Turkey, India, and Japan.

Under the MOU, Commerce will continue to lead bilateral and multilateral negotiations on policy matters dealing with exports and will still have the jurisdiction responsibility for export enforcement policy. There have been four meetings at the Deputy Assistant Secretary level to facilitate the implementation of the MOU which would require the exchanging of lists of cases under investigation; the exchange of cable traffic; guidance for U.S. foreign posts has been sent out to all foreign posts, specifically including the MOU, and the way it will be implemented.

As the President has pointed out, both Commerce and Customs bring important complementary strengths to export enforcement. Commerce has been enforcing the act since 1949. Its Office of Export Enforcement is a single mission agency whose sole responsibility and function being the enforcement of the Export Adminis-

tration Act. Furthermore, Commerce has, under one roof, both the licensing and enforcement functions. This symbiotic relationship benefits both the technical licensing experts at the time of licensing decisions and enforcement agents in meeting their responsibilities under the EAA.

Though the MOU does not deal with all aspects of EAA enforcement, it certainly should lead to a closer relationship between Commerce and Customs across the board. This cooperation will increase efficiency and produce a more effective U.S. Government response to the threat to our national security and foreign policy interests that stems from the illegal exportation of our critical technology.

With respect to the *MRI* case, I'd like to comment at the outset that the Commerce Department made mistakes in the handling of that case. I might add, Mr. Chairman, in terms of your suggestion, there was some difficulty because of some of the sensitivity of the information, to have a public statement. Also, we have the problem of business confidential information.

The mistakes were as follows:

One, inadequately disseminating and analyzing the sensitive intelligence information received by the Compliance Division, OEE's predecessor, in May 1980. It should be noted that this same information was received by both the Defense and Treasury Departments. The Commerce agent was provided incomplete information which precluded subsequent proper investigation of the case.

Two, the Compliance Division's failure to start an investigation into MRI until about 1 year after the above-mentioned negative information was received.

Three, neglecting to put MRI and Semitronics, a firm owned by Mr. Mueller, into the investigative index file under this original investigation. This index file is important because it is a reference source for past case records, and that's the important thing, that when a case is originally opened several prelicensing and postshipment checks were done and there was nothing but positive and in fact laudatory statements coming out of our counsel general's office in Capetown. The case was closed. But when further information came in about 1 year later, the new case agent did not know that there was a previous case on MRI and that there was previous intelligence information on the case.

I would also add at this point that the person receiving the information within the Commerce Department and supplying it to the Compliance Division about 2 months after the information came was transferred on an interagency basis on a detail for a little over 1 year to the State Department and was no longer handling the case.

Finally, two other points were that I think Commerce failed to quickly reopen the *MRI* case for priority investigation upon receipt of a letter from a U.S. firm, reporting that MRI had not requested installation services on certain equipment exported to MRI.

And finally, neglecting to put MRI on the licensing screen which is used to screen license applications.

I think that it's important to note, before going on with the aspects of Commerce's improvement in the enforcement program, to note the context of the situation regarding MRI particularly in

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May 1980. In May 1980, the Commerce Department at that point in time had 12 criminal investigators, some of which one might argue were not highly trained.

The second point that would be made about it in terms of the context is that in May 1980 as a result of over a decade by the U.S. Government of basically ignoring, if not ignoring a lack of emphasis, on the entire export control program, not just within the Commerce Department but in fact in all other agencies involved in export control.

I at the time, in 1980, was Deputy Commissioner of Customs. The Export Administration activities at that time were not a priority of the administration and they were not a priority of the Treasury Department, and I think that there's a tendency at times to have the notion be that it's only at the Commerce Department where there was a lack of emphasis on the export control program. I think that my experience has been that the entire Government failed to take seriously the implementation of the Export Administration Act, particularly in the enforcement aspects.

Also, at this point in time, the Commerce Department failing to have what we thought were people who were adequately trained and enough people to do the job, a number of professional investigative activities were not undertaken. Specifically, there was little capability within the Department for a systematic review of intelligence information. We also understand that this was true really across the board because it's been my experience in the last 18 months in this job that the intelligence apparatus of the United States has improved dramatically from what it was 3 years ago.

SHORTCOMINGS IN THE OFFICE OF COMPLIANCE

I'd also like to note that when the new administration came in in 1981 it was readily apparent that there was clear shortcomings in the Office of Compliance. Secretary Baldrige and Under Secretary Olmer both acknowledged these shortcomings and directed that they be dealt with. Under Secretary Olmer asked the Inspector General's Office to conduct an investigation of the Compliance Division in early 1982. While awaiting the IG's report, the Department took immediate actions to strengthen the enforcement program.

Specifically, the Compliance Division was expanded and made into an Office of Export Enforcement [OEE] headed by a newly created Deputy Secretary for Enforcement. Mr. Ted Wu, a former assistant U.S. attorney with extensive recent customs and export control investigation and prosecution experience, was appointed in July 1982 to fill that position. He was directed to identify the problems that he saw in the enforcement program. He concluded that the program had a number of deficiencies as follows: One, lack of effective overall enforcement strategy to address the Nation's technology leakage problem; two, an insufficient number of trained personnel; three, inadequate management direction and oversight; four, lack of strong leadership and clear lines of organizational responsibility, and five, little, if any, emphasis on systematic application of modern intelligence or investigative techniques; inadequate cooperation and coordination with the U.S. intelligence community

and U.S. enforcement agencies; and overall, inadequate travel funds.

Since that time we've done a lot to improve the enforcement program. Today, OEE has over 45 experienced criminal investigators and 20 intelligence analysts personnel, in addition to some 30 other staff personnel. In September 1982, we opened new offices in Los Angeles and San Francisco. The existing New York field staff and the Washington headquarters staff have been further strengthened. Further, at the specific request of American embassies in Sweden and Austria, one OEE investigator has been detailed to each of those embassies to provide export control and enforcement support.

Plans for six new field offices in important technology centers within the United States have been completed. This added expansion is awaiting congressional approval of the necessary additional funding. If approved, we will have 99 investigators, 24 intelligence analysts, and 49 support personnel by the end of this year.

The second area we've improved is in the area of training. All of our agents have gone through, if they hadn't already, the Federal Law Enforcement Training Center and we've also developed for our agents a special 2-week program just dealing with export control and the Export Administration Act.

I've alluded to some of the improvements in the intelligence operations. I might also note in conjunction with Commerce's export licensing arm, with the Office of Export Administration, OEE has developed and implemented an automated licensing screen. This screen contains the names of over 4,300 suspect companies and individuals. All license applications are screened twice—first, upon initial receipt, and second, immediately prior to the actual issuance of a license. The last step insures that the most current listing on the screen is applied prior to the license issuance.

I would note, Mr. Chairman, that that was one of the issues with MRI. When the MRI—the VAX application in house came in in September 1982. We got information in late November 1982 from a private company suspecting some unusual circumstances. At that point in time, if a case was already in, the screen had already taken place. Therefore, the enforcement people, if additional negative information came in, the people in the enforcement or licensing side would not have known that. That's one of the reasons now through the computer, not once but twice, we now do a screen to allow if late events occur, late information comes in before it's licensed, then negative information is known by both the licensing people and the enforcement people.

With these increased resources OEE has also been able to respond much more fully to the need for information necessary to prevent the issuance of export licenses in situations where the contemplated export poses a high diversion risk. During the last 18 months of OEE operations, Commerce initiated 622 prelicense checks and 55 postshipment verification inquiries. OEA rejected 78 export license applications, amounting to more than $62 million of controlled commodities. The automated licensing screen and other management improvements have enabled us to dramatically increase the number of license applications receiving enforcement scrutiny. For example, for the first 3 months of 1984, the monthly

average number of applications reviewed by OEE has increased 184 percent, compared to the average for the previous year. To make even more effective use of the intelligence and exporting information available to Commerce, OEE and OEA have formed a joint intelligence analytical team to analyze this information and guide licensing and enforcement activities.

We have also entered into a memorandum of understanding with the FBI, Defense Intelligence Agency, CIA, and the U.S. Customs Service, to establish procedures for coordination, cooperation, and information exchange relating to strategic export controls. I might note that none of these were in place during the time all of the MRI incident occurred.

We are also very involved and been in on all the details in terms of the CoCom multilateral enforcement efforts.

MARKED IMPROVEMENT BY OEE OVER PRECEDING 3-YEAR PERIOD

Finally, I would like to note some aspects regarding outputs. In fiscal year 1983, OEE referred 37 cases to the Justice Department for possible criminal prosecution, compared to 16 cases in the entire 3-year period preceding 1983. The convictions of seven EAA violators in fiscal year 1983 resulting from OEE's investigative action stands in marked contrast to the same number of convictions obtained during the entire 3-year period preceding fiscal year 1983.

Thus far, in the first 6 months of fiscal year 1984, OEE has referred 28 cases to the Justice Department and indictments have been obtained against 12 defendants. Five defendants have been convicted. At present, OEE is pursuing approximately 755 cases of possible export violations. Many of these investigations, like those cases that have already been prosecuted, concern elaborate and complicated diversion schemes and criminal conspiracies involving suspects both here and abroad.

Finally, other enforcement activity by OEE led to the initiation of administrative actions affecting 70 separate parties in the United States and overseas. These administrative measures were in the form of temporary denial orders and final orders denying export privileges, and the imposition of civil fines. Commerce's unique ability to take these actions is a potent enforcement weapon for preventing sensitive U.S.-origin goods from falling into the hands of known or suspected diverters, particularly those outside the U.S. jurisdiction and thus beyond the reach of the American criminal process. Although no other Federal enforcement agency has utilized this unique preventive export enforcement tool, we encourage their participation.

Finally, also in terms of OEE and the private sector, I think there's one factor—and I won't read all of it—but from July 1982 to February 1984, 431 investigations were opened by the Office of Export Enforcement as a result of leads provided by the business community. We think that's a direct result of the fact that what we have provided to thousands of individuals through our export control seminar programs have considerably heightened the sensitivity of the American export community and I think the result of

that is going to be a tremendous increase in the number of tips provided by the business community.

I'd like to just finish by noting several aspects about the *MRI* case. I've noted some of the mistakes that I think the Commerce Department made. Specifically, with respect to the VAX diversion case, when the information came to the Government's attention in March 1980, it first came to our attention in March 1980 when a U.S. firm applied for an export license to ship an ion implantation system to MRI. Commerce's Compliance Division appropriately requested a routine prelicense check. On May 12, 1980, the consulate general reported that MRI was a suitable recipient of U.S.-origin high technology. The counsel general based its recommendation on an interview with MRI's director and on a favorable "World Traders Data Report," similar to Dun and Bradstreet.

On May 16, 1980, Commerce, Defense, and Treasury all were given highly sensitive information requiring special handling indicating that Semitronic AG, a firm known to be owned by the diverter Richard Mueller, was interested in purchasing U.S.-origin semiconductor manufacturing systems through MRI for eventual resale, possibly to the U.S.S.R.

The notations made by the Compliance Division agent with access to this information were interpreted to indicate that MRI was the company divulging the information and, consequently, the lead was not given priority attention. In addition, this agent, as I've noted already, was detailed to the State Department for 1 year and not available to follow up within the Compliance Division on the processing of this lead. Similar highly sensitive information was provided to Commerce and other agencies on April 23, June 26, and July 21, 1980, but these were never received by the Office of Export Enforcement in the Compliance Division at that time.

After receipt of the May 16, 1980 information, the Compliance Division requested two postshipment checks by the consulate general and reviewed Commerce licensing data on MRI. On November 17, 1981, and February 25, 1982, the consulate general reported favorably on MRI, an onsite visit having been made by a consulate general official. The consulate general reports, therefore, did not corroborate the negative information we received on May 16.

Let me stress that the consulate general's office never conveyed any unfavorable information to us regarding MRI, nor did they ever report any connection between MRI and Richard Mueller. In fact, the financial information provided us by the South African Government never indicates Richard Mueller's ownership in this company. In fact, between April 1980 and May 1983, the consulate general reported to us that MRI and Dr. Harrison, the managing director, were reliable recipients of U.S. technology and recommended issuance of export licenses.

For example, on September 23, 1982, the consulate general responded to one of our four prelicense checks stating that:

> Consulate general has known Dr. Harrison and his institute for several years and considers them reliable recipients of sensitive U.S. equipment. Therefore recommend issuance of license.

Indeed, as recently as May 26, 1983, when it was obvious there were serious issues involving MRI, the consulate general responded favorably to another MRI prelicense check request stating:

> Post has had numerous contacts with Dr. Harrison in the past few years * * * and we consider his firm a reliable trading partner for U.S. firms.

FAVORABLE REPORTS MINIMIZED OTHER INFORMATION

These favorable reports served to minimize the importance of other information we received, such as a November 29, 1982 letter from a U.S. firm reporting that MRI had failed to request installation of some very sophisticated semiconductor manufacturing equipment. The company in the same letter said, although this is unusual because if the company who made it didn't install it, they at the same time stated that there was an engineer working for MRI who was in training by the company producing the equipment and he was the best engineer in the training program and he was fully capable of actually installing the devices.

The problem was that that was on November 29. The case was opened on December 14 and was not transferred to the field until March. During that period of time, between November 29 and March, the VAX case had come in on September 19, 1982, had been returned because of lack of sufficient information about the power of the computer, had been reviewed, come back in and reviewed by the Department of Energy, and it was licensed on December 30, 1982. It was another license that was also licensed in December which was the last one that was licensed for MRI. There were two subsequent applications that were rejected or rescinded during 1983.

Other information, I might note, we received also contributed to MRI's appearance of legitimacy. Again, in May 1983, OEE received information from another very major firm which had sold a very large package of semiconductor equipment to MRI that one of their engineers in April 1983 had visited MRI and reported that MRI had special clean rooms for the equipment it had purchased from the U.S. firm, that additional clean rooms were being prepared as well as other preparations, and that the technician had seen a huge digital equipment computer being used by MRI to manufacture integrated circuits.

Mr. Chairman, the importance of realizing mistakes is to effectuate solutions so that similar mistakes don't happen again. I think we are doing that now in terms of some of the things I've already alluded to. We have dramatically increased from 2 to 19 people the Office of Intelligence Assessment in which instead of one person dealing with sensitive information there is a group leader and a team of people who look at it every day.

Second, the automated screen with the dual screening of applications has eliminated the problem we had of the lack of coordination between OEA and OEE.

Finally, all cases are put into the name data file. In fact, the chief of the intelligence division who refers cases for investigation also has the cases automatically added to the computerized licensing screen.

Mr. Chairman, given the constraints of an open session, I have tried to be as forthright as possible regarding the *MRI* case and to convey to you the fact that the Commerce Department's enforcement program has improved considerably in the last 2 years and will be improving even more in the near future. Commerce feels strongly that we can more than fulfill the confidence of the President in his decision of 2 weeks ago when he stated that the Commerce Department and the Customs Service together do, indeed, bring important complementary assets to the enforcement of the Export Administration Act.

Thank you.

The CHAIRMAN. Thank you, Mr. Archey.

[The complete statement follows:]

TESTIMONY OF WILLIAM T. ARCHEY, ACTING ASSISTANT SECRETARY FOR TRADE ADMINISTRATION, DEPARTMENT OF COMMERCE

MR. CHAIRMAN, I AM PLEASED TO APPEAR TODAY TO EXPLAIN THE RECENT MEMORANDUM OF UNDERSTANDING (MOU) BETWEEN COMMERCE AND TREASURY RELATING TO ENFORCEMENT OF THE EXPORT ADMINISTRATION ACT (EAA), TO DISCUSS THE MRI CASE, AND TO DESCRIBE THE SIGNIFICANT IMPROVEMENTS COMMERCE HAS MADE IN ITS EXPORT ENFORCEMENT PROGRAM.

ON JANUARY 16, 1984, LIONEL OLMER, UNDER SECRETARY OF COMMERCE FOR INTERNATIONAL TRADE, AND JOHN WALKER, ASSISTANT SECRETARY OF TREASURY FOR ENFORCEMENT AND OPERATIONS, SIGNED AN MOU RELATING TO THE CONDUCT OF EAA INVESTIGATIONS OVERSEAS. TWO WEEKS AGO, THE PRESIDENT PERSONALLY ENDORSED THE MOU, AND FURTHER CONCLUDED THAT CUSTOMS AND COMMERCE BRING IMPORTANT COMPLEMENTARY ASSETS TO THE ENFORCEMENT OF THE EAA.

THE MOU PRIMARILY DEALS WITH THE OVERSEAS ASPECTS OF EAA INVESTIGATIONS. THE MOU PROVIDES THAT BOTH COMMERCE (THROUGH ITS OFFICE OF EXPORT ENFORCEMENT) AND TREASURY (THROUGH THE U.S. CUSTOMS SERVICE) WILL CONTINUE TO CONDUCT THEIR OWN INVESTIGATIONS OVERSEAS. THE MOU CLARIFIES WHO WILL INITIATE THE CONTACT ABROAD WITH FOREIGN ENFORCEMENT AGENCIES. THIS LIAISON FUNCTION WILL BE THE RESPONSIBILITY OF THE CUSTOMS SERVICE IN MOST COUNTRIES. HOWEVER, IN THOSE COUNTRIES WHERE THE HOST GOVERNMENT HAS ESTABLISHED THE EXPORT CONTROL ENFORCEMENT FUNCTION IN A TRADE DEPARTMENT, COMMERCE WILL PROVIDE ITS OWN LIAISON.

CURRENTLY, THE COUNTRIES WHICH ARE DESIGNATED UNDER THE MOU AS ONES IN WHICH COMMERCE WILL PROVIDE ITS OWN INITIAL LIAISON ARE

SWEDEN, BELGIUM, AUSTRIA, TURKEY, INDIA, AND JAPAN. THIS LISTING COULD BE MODIFIED IN THE FUTURE AS MAY BE APPROPRIATE.

THE MOU EMPHASIZES THE EXCLUSIVE JURISDICTION AND RESPONSIBILITY OF COMMERCE IN EXPORT ENFORCEMENT POLICY. COMMERCE WILL CONTINUE TO LEAD BILATERAL AND MULTILATERAL NEGOTIATIONS ON POLICY MATTERS.

COMMERCE AND TREASURY HAVE HAD FOUR MEETINGS AT THE DEPUTY ASSISTANT SECRETARY LEVEL TO FACILITATE THE IMPLEMENTATION OF THE MOU. THERE HAVE BEEN SEVERAL MORE MEETINGS AT THE WORKING LEVEL. MUCH HAS BEEN DONE IN THE IMPLEMENTATION OF THE AGREEMENT. FOR EXAMPLE:

- EXCHANGE LISTS OF OPEN CASES UNDER INVESTIGATION: THIS WILL IMPROVE COORDINATION AND MINIMIZE UNNECESSARY REDUNDANT EFFORTS. FURTHER, OUR RECEIPT OF INFORMATION FROM CUSTOMS CASES IS OF CRITICAL IMPORTANCE IN COMMERCE'S REVIEW OF EXPORT LICENSE APPLICATIONS.

- EXCHANGE OF CABLE TRAFFIC: THIS IS BUT ONE OF SEVERAL STEPS THE AGENCIES HAVE IMPLEMENTED TO KEEP EACH OTHER INFORMED ABOUT WHAT THEY ARE DOING OVERSEAS.

- GUIDANCE FOR U.S. FOREIGN POSTS: A CABLE EXPLAINING THE MOU HAS BEEN TRANSMITTED TO ALL FOREIGN POSTS.

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COMMERCE, FOR ITS PART, IS FIRMLY COMMITTED TO FAITHFUL IMPLEMENTATION OF THE MOU. WE BELIEVE THAT GOOD FAITH AND VIGOROUS EXECUTION OF THE AGREEMENT WILL LEAD TO A MORE EFFECTIVE OVERALL ENFORCEMENT EFFORT.

AS THE PRESIDENT HAS POINTED OUT, BOTH COMMERCE AND CUSTOMS BRING IMPORTANT COMPLEMENTARY STRENGTHS TO EXPORT ENFORCEMENT. COMMERCE HAS BEEN ENFORCING THE EAA SINCE 1949. ITS OFFICE OF EXPORT ENFORCEMENT (OEE) IS A SINGLE MISSION AGENCY WHOSE SOLE RESPONSIBILITY AND FUNCTION IS THE ENFORCEMENT OF THE EAA. FURTHER, COMMERCE HAS, UNDER ONE ROOF, BOTH THE LICENSING AND ENFORCEMENT FUNCTIONS. THIS SYMBIOTIC RELATIONSHIP BENEFITS BOTH THE TECHNICAL LICENSING EXPERTS AND ENFORCEMENT AGENTS IN MEETING THEIR RESPONSIBILITIES UNDER THE EAA. U.S. CUSTOMS, ON THE OTHER HAND, BRINGS ITS SIZE, GEOGRAPHIC DISPERSION, AND INSPECTION FORCE TO EXPORT CONTROL ENFORCEMENT. COMMERCE AND CUSTOMS TOGETHER CAN DO FAR MORE THAN EITHER CAN ALONE.

THOUGH THE MOU DOES NOT DEAL WITH ALL ASPECTS OF EAA ENFORCEMENT, IT WILL LEAD TO A CLOSER RELATIONSHIP BETWEEN COMMERCE AND CUSTOMS ACROSS THE BOARD. THIS COOPERATION WILL INCREASE EFFICIENCY AND PRODUCE A MORE EFFECTIVE U.S. GOVERNMENT RESPONSE TO THE THREAT TO OUR NATIONAL SECURITY AND FOREIGN POLICY INTERESTS THAT STEMS FROM THE ILLEGAL EXPORTATION OF OUR CRITICAL TECHNOLOGY.

MR. CHAIRMAN, WITH RESPECT TO THE MRI CASE OF ATTEMPTED DIVERSION, I WANT TO ACKNOWLEDGE AT THE VERY OUTSET THAT THE COMMERCE

DEPARTMENT MADE MISTAKES IN THE HANDLING OF THAT CASE. BASICALLY, THE MISTAKES WE MADE WERE:

- INADEQUATELY DISSEMINATING AND ANALYZING THE SENSITIVE INTELLIGENCE RECEIVED BY THE COMPLIANCE DIVISION, OEE'S PREDECESSOR, IN MAY 1980. IT SHOULD BE NOTED THAT THIS SAME INFORMATION WAS RECEIVED BY BOTH THE DEFENSE AND TREASURY DEPARTMENTS. THE COMMERCE CASE AGENT WAS PROVIDED INCOMPLETE INFORMATION WHICH PRECLUDED SUBSEQUENT PROPER INVESTIGATION OF THE CASE.

- THE COMPLIANCE DIVISION'S FAILURE TO START AN INVESTIGATION INTO MRI UNTIL ONE YEAR AFTER THE ABOVE MENTIONED NEGATIVE INFORMATION WAS RECEIVED.

- NEGLECTING TO PUT MRI AND SEMITRONICS, A FIRM OWNED BY A KNOWN DIVERTER, RICHARD MUELLER, INTO THE INVESTIGATIVE INDEX FILE UNDER THIS ORIGINAL INVESTIGATION. THIS INDEX FILE IS IMPORTANT BECAUSE IT IS A REFERENCE SOURCE FOR PAST CASE RECORDS.

- NEGLECTING TO QUICKLY RE-OPEN THE MRI CASE FOR PRIORITY INVESTIGATION UPON RECEIPT OF A LETTER FROM A U.S. FIRM, REPORTING THAT MRI HAD NOT REQUESTED INSTALLATION SERVICES ON CERTAIN EQUIPMENT EXPORTED TO MRI.

- o Upon re-opening of the case in December 1982, neglecting to put MRI on the licensing screen, which is used to screen license applications.

Mr. Chairman, before I get into a contextual discussion of how these mistakes could have happened, I want to convey to you the state of affairs existing in Commerce's Compliance Division in the 1980 to mid-1982 timeframe.

Under three previous administrations little attention was given by the Government to the U.S. export control program. As a result, the Department of Commerce's export enforcement arm -- the then Compliance Division -- was allowed to atrophy and shrink over the years. After assuming office, both Secretary Baldrige and Under Secretary Olmer recognized the serious shortcomings of the Compliance Division. Clearly, that office which only had twelve criminal investigators and 2 intelligence analysts, was inadequate to meet Commerce's enforcement responsibilities. The Under Secretary, therefore, asked the Inspector General to conduct an investigation of the Compliance Division.

The Department, while awaiting the IG's report, took immediate steps to strengthen the enforcement program. Specifically, the Compliance Division was expanded and made into the Office of Export Enforcement, headed by a newly-created deputy assistant secretary post.

TED WU, A FORMER ASSISTANT U.S. ATTORNEY WITH EXTENSIVE, RECENT CUSTOMS AND EXPORT CONTROL INVESTIGATION AND PROSECUTION EXPERIENCE, WAS APPOINTED IN JULY 1982 TO FILL THAT POSITION. HE WAS DIRECTED TO IDENTIFY AND RESOLVE PROBLEMS WHICH HE PERCEIVED IN THE ENFORCEMENT PROGRAM. WU CONCLUDED THAT THE DEPARTMENT'S PROGRAM HAD A NUMBER OF DEFICIENCIES, INCLUDING:

- LACK OF AN EFFECTIVE OVERALL ENFORCEMENT STRATEGY TO ADDRESS THE NATION'S TECHNOLOGY LEAKAGE PROBLEM;

- AN INSUFFICIENT NUMBER OF TRAINED PERSONNEL;

- INADEQUATE MANAGEMENT DIRECTION AND OVERSIGHT;

- LACK OF STRONG LEADERSHIP AND CLEAR LINES OF ORGANIZATIONAL RESPONSIBILITY;

- LITTLE, IF ANY, EMPHASIS AND GUIDANCE ON THE SYSTEMATIC APPLICATION OF MODERN INTELLIGENCE OR INVESTIGATIVE TECHNIQUES, RESOURCES AND SYSTEMS;

- INADEQUATE COOPERATION AND COORDINATION WITH THE U.S. INTELLIGENCE COMMUNITY AND U.S. ENFORCEMENT AGENCIES; AND,

- INADEQUATE TRAVEL FUNDS, LAW ENFORCEMENT EQUIPMENT AND OTHER SUPPORT RESOURCES.

MR. CHAIRMAN, WE'VE DONE A LOT TO IMPROVE OUR ENFORCEMENT PROGRAM. WE RECOGNIZE MUCH MORE NEEDS TO BE DONE, I WOULD LIKE TO RECAP BRIEFLY FOR YOU OUR EFFORTS TO DATE AND THE PAYOFFS WE ARE GETTING.

INCREASED STAFFING & NUMBER OF FIELD OFFICE

TODAY, OEE HAS OVER 45 EXPERIENCED CRIMINAL INVESTIGATORS AND 20 INTELLIGENCE ANALYSTS/SUPPORT PERSONNEL, IN ADDITION TO SOME 30 OTHER STAFF PERSONNEL. IN SEPTEMBER 1982 NEW FIELD OFFICES WERE OPENED IN LOS ANGELES AND SAN FRANCISCO. THE EXISTING NEW YORK FIELD STAFF AND THE WASHINGTON HEADQUARTERS STAFF HAVE BEEN STRENGTHENED. FURTHER, AT THE SPECIFIC REQUEST OF AMERICAN EMBASSIES IN SWEDEN AND AUSTRIA, ONE OEE INVESTIGATOR HAS BEEN DETAILED TO EACH OF THOSE EMBASSIES TO PROVIDE EXPORT CONTROL AND ENFORCEMENT SUPPORT.

TO SUPPORT THIS EXPANSION EFFORT, COMMERCE INCREASED THE ENFORCEMENT BUDGET FROM $1.8 MILLION FOR FY 81 TO $3.6 MILLION FOR FY 83. THIS INCREASED LEVEL OF FUNDING PROVIDED FOR THE EXPANDED STAFF, NEW FIELD OFFICES AND THE NECESSARY TRAVEL, TRAINING, SUPPLIES AND EQUIPMENT NEEDS OF THIS EXPANDED STAFF AND INCREASED LEVEL OF ACTIVITIES.

PLANS FOR 6 NEW FIELD OFFICES IN IMPORTANT TECHNOLOGY CENTERS WITHIN THE U.S. HAVE BEEN COMPLETED. THIS ADDED EXPANSION IS

AWAITING CONGRESSIONAL APPROVAL OF THE NECESSARY ADDITIONAL FUNDING. IF APPROVED, WE WILL HAVE 99 INVESTIGATORS, 24 INTELLIGENCE ANALYSTS, AND 49 SUPPORT PERSONNEL BY THE END OF THIS FISCAL YEAR.

RECRUITMENT AND TRAINING

DURING OUR STAFF EXPANSION, EMPHASIS WAS PLACED ON MAINTAINING THE HIGHEST POSSIBLE CALIBRE OF PROFESSIONAL INVESTIGATORS THROUGH THE HIRING OF ONLY EXPERIENCED, TESTED CRIMINAL INVESTIGATORS.

WE HAVE ALSO DESIGNED AND IMPLEMENTED SPECIALIZED STRATEGIC EXPORT ENFORCEMENT TRAINING FOR OUR SPECIAL AGENTS. THIS FORMAL ADVANCED PROFESSIONAL TRAINING IS IN ADDITION TO THE SPECIAL AGENTS' BASIC FEDERAL LAW ENFORCEMENT TRAINING RECEIVED BY ALL FEDERAL AGENTS.

IMPROVED INTELLIGENCE OPERATIONS

OEE'S INTELLIGENCE FUNCTION IS A KEY COMPONENT OF THE DEPARTMENT'S STRATEGIC TRADE ENFORCEMENT PROGRAM. OEE'S INTELLIGENCE DIVISION USES INTELLIGENCE COLLECTED AND PROCESSED BY THE INTELLIGENCE COMMUNITY AND OTHER AGENCIES, AS WELL AS BY COMMERCE ITSELF. THE STAFF HAS BEEN TRIPLED AND AUTOMATED DATA PROCESSING SYSTEMS ARE BEING USED FOR THE PROCESSING, ANALYSIS AND APPLICATION OF EXPORT CONTROL INTELLIGENCE.

IN CONJUNCTION WITH COMMERCE'S EXPORT LICENSING ARM, THE OFFICE OF EXPORT ADMINISTRATION (OEA), OEE HAS DEVELOPED AND IMPLEMENTED AN AUTOMATED LICENSING SCREEN. THIS SCREEN CONTAINS THE NAMES OF OVER 4300 SUSPECT COMPANIES AND INDIVIDUALS. ALL LICENSE APPLICATIONS ARE SCREENED TWICE -- FIRST, UPON INITIAL RECEIPT, AND SECOND, IMMEDIATELY PRIOR TO THE ACTUAL ISSUANCE OF A LICENSE. THE LAST STEP INSURES THAT THE MOST CURRENT LISTING ON THE SCREEN IS APPLIED PRIOR TO THE LICENSE ISSUANCE.

WITH THESE INCREASED RESOURCES OEE HAS ALSO BEEN ABLE TO RESPOND MORE FULLY TO OEA'S NEED FOR INFORMATION NECESSARY TO PREVENT THE ISSUANCE OF EXPORT LICENSES IN SITUATIONS WHERE THE CONTEMPLATED EXPORT POSES A HIGH DIVERSION RISK. DURING THE LAST EIGHTEEN MONTHS OF OEE OPERATIONS, COMMERCE INITIATED 622 PRE-LICENSE CHECKS AND 55 POST-SHIPMENT VERIFICATION INQUIRIES. OEA REJECTED SEVENTY-EIGHT EXPORT LICENSE APPLICATIONS, AMOUNTING TO MORE THAN $62 MILLION OF CONTROLLED COMMODITIES ON OEE'S RECOMMENDATIONS WHICH, IN TURN, WERE BASED ON ADVERSE PRE-LICENSE OR POST-SHIPMENT FINDINGS OR SENSITIVE INTELLIGENCE THAT IMPLICATED PROBABLE RISK TO NATIONAL SECURITY. THE AUTOMATED LICENSING SCREEN AND OTHER MANAGEMENT IMPROVEMENTS HAVE ENABLED US TO DRAMATICALLY INCREASE THE NUMBER OF LICENSE APPLICATIONS RECEIVING ENFORCEMENT SCRUTINY. FOR EXAMPLE, FOR THE FIRST THREE MONTHS OF 1984, THE MONTHLY AVERAGE NUMBER OF APPLICATIONS REVIEWED BY OEE HAS INCREASED 184%, COMPARED TO THE AVERAGE FOR THE PREVIOUS YEAR.

TO MAKE EVEN MORE EFFECTIVE USE OF THE INTELLIGENCE AND EXPORTING INFORMATION AVAILABLE TO COMMERCE, OEE AND OEA HAVE FORMED A JOINT INTELLIGENCE ANALYTICAL TEAM TO ANALYZE THIS INFORMATION AND GUIDE LICENSING AND ENFORCEMENT ACTIVITIES.

INTERAGENCY COORDINATION

COMMERCE HAS ENTERED INTO MEMORANDA OF UNDERSTANDING (MOU) WITH THE FBI, DIA, CIA AND THE U.S. CUSTOMS SERVICE, WHICH ESTABLISH PROCEDURES FOR COORDINATION, COOPERATION AND INFORMATION EXCHANGE RELATING TO STRATEGIC EXPORT CONTROLS. WE ARE ALSO IN THE PROCESS OF FINALIZING A MOU WITH THE NATIONAL SECURITY AGENCY.

COCOM MULTILATERAL ENFORCEMENT EMPHASIS

SINCE FEBRUARY 1983, OEE HAS PLAYED A LEADERSHIP ROLE IN COCOM EXPORT CONTROL ENFORCEMENT EFFORTS. TED WU, IN CONJUNCTION WITH THE STATE DEPARTMENT, HAS LED OVER 15 EXPORT CONTROL ENFORCEMENT BILATERALS WITH 9 COCOM COUNTRIES OR FRIENDLY NON-ALIGNED COUNTRIES. IN ADDITION, WE HAVE INSTITUTED EXPORT CONTROL EXCHANGE VISITS WITH THE UNITED KINGDOM AND JAPAN. RECENTLY, OEE WORKED CLOSELY WITH BELGIAN EXPORT CONTROL AUTHORITIES AND SUCCEEDED IN HELPING THE BELGIAN GOVERNMENT INVESTIGATE A MAJOR U.S.-BELGIUM DIVERSION TO THE EASTERN BLOC.

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OEE PERFORMANCE

In fiscal year (FY) 1983, OEE referred 37 EAA cases to the Justice Department for possible criminal prosecution, compared to just 16 cases referrals for the entire three-year period preceding FY 83. The convictions of 7 EAA violators in FY 83 resulting from OEE investigative action stands in marked contrast to the same number of convictions obtained during the entire three-year period preceding FY 83.

Thus far in the first six months of FY 84, OEE has referred 28 cases to the Justice Department and indictments have been obtained against 12 defendants. Five defendants have been convicted. At present, OEE is pursuing approximately 755 cases of possible export violations. Many of these investigations, like those cases that have already been prosecuted, concern elaborate and complicated diversion schemes and criminal conspiracies involving suspects both here and abroad.

Other enforcement activity by OEE in FY 83 led to the initiation of administrative actions affecting 70 separate parties in the U.S. and overseas. These administrative measures were in the form of temporary denial orders and final orders denying export privileges, and the imposition of civil fines. Commerce's unique ability to take these administrative actions is a potent enforcement weapon for preventing sensitive U.S.-origin goods from

FALLING INTO THE HANDS OF KNOWN OR SUSPECTED DIVERTERS, PARTICULARLY THOSE OUTSIDE THE U.S. JURISDICTION AND THUS BEYOND THE REACH OF THE AMERICAN CRIMINAL PROCESS. ALTHOUGH NO OTHER FEDERAL ENFORCEMENT AGENCY HAS UTILIZED THIS UNIQUE PREVENTIVE EXPORT ENFORCEMENT TOOL, WE ENCOURAGE THEIR PARTICIPATION.

UNDER OEE'S LIMITED CARGO INSPECTION PROGRAM, OUR FIVE OEE INSPECTORS CONDUCTED 8,912 CARGO EXAMINATIONS IN FY 83, RESULTING IN THE ADMINISTRATIVE SEIZURE OF 238 SHIPMENTS VALUED AT APPROXIMATELY $5.4 MILLION. DURING THIS SAME PERIOD AS A RESULT OF THE ENFORCEMENT SCREENING OF LICENSE APPLICATIONS, OEE SELECTIVELY REVIEWED 5,743 EXPORT LICENSE APPLICATIONS TO IDENTIFY SUSPECT TRANSACTIONS. THESE APPLICATIONS WERE SCRUTINIZED IN-HOUSE FOR POSSIBLE INDICIA OF POTENTIAL DIVERSION OR OTHER ILLEGAL DISPOSITION OF U.S.-ORIGIN COMMODITIES OR TECHNOLOGY.

OEE AND THE PRIVATE SECTOR

SOON AFTER ITS INCEPTION, OEE EMBARKED ON A MAJOR PUBLIC AWARENESS CAMPAIGN. IN THE PAST 16 MONTHS, COMMERCE ENFORCEMENT PERSONNEL HAVE MADE PRESENTATIONS TO OVER 1,200 FIRMS AND TRADE ASSOCIATIONS ACROSS THE UNITED STATES AS WELL AS EUROPE AND SCANDINAVIA ON EXPORT CONTROL ISSUES. OEE HAS ALSO PUBLISHED AND CIRCULATED IN THE U.S. AND EUROPE A LIST OF "RED FLAG" INDICATORS WHICH SIGNAL POSSIBLE ILLEGAL EXPORT OR DIVERSIONS.

IN JANUARY, 1984, OEE PUBLISHED A LIST OF "HELPFUL HINTS" TO ASSIST EXPORTERS TO COMPLY WITH U.S. EXPORT CONTROLS. THESE PUBLICATIONS ARE BEING USED AND HAVE BEEN DISTRIBUTED BY GOVERNMENT AGENCIES AND BUSINESS COMMUNITIES HERE AND ABROAD.

FROM JULY, 1982 THROUGH FEBRUARY 1984, 431 INVESTIGATIONS WERE OPENED BY OEE AS A RESULT OF LEADS PROVIDED BY THE BUSINESS COMMUNITY. HENCE, THE PUBLIC PLAYS AN IMPORTANT PARTNERSHIP ROLE IN OUR ENFORCEMENT PROGRAM.

RETURNING TO THE MRI/VAX DIVERSION CASE, MR. CHAIRMAN, IN HINDSIGHT I CAN SAY THAT WHILE WE DID MAKE MISTAKES, WE ALSO DID MANY THINGS PROPERLY. FOR EXAMPLE:

ALTHOUGH THE COMPLIANCE DIVISION DID NOT ACT QUICKLY IN 1980 UPON THE INITIAL RECEIPT OF NEGATIVE INFORMATION CONCERNING MRI, TWO IMPORTANT FACTS SHOULD BE KEPT IN MIND: (1) THE INFORMATION CONVEYED TO THE CASE AGENT WAS NOT CLEAR, GIVING THE IMPRESSION THAT MRI WAS THE SOURCE OF THE INFORMATION, HENCE, PSYCHOLOGICALLY CASTING MRI IN A "GOOD GUY" ROLE; (2) EVEN IN THE ABSENCE OF AN INVESTIGATION ON MRI, PROPOSED EXPORTS OF SENSITIVE COMMODITIES TO THAT COMPANY WERE BEING PROPERLY MONITORED THROUGH THE NORMAL PRE-LICENSE CHECK MECHANISM. THE PURPOSE OF SUCH CHECKS INCLUDES ESTABLISHING THE BONA FIDES OF THE RECIPIENT, THE NATURE OF ITS BUSINESS, AND WHETHER THE PROPOSED U.S. EXPORT IS APPROPRIATE.

SPECIFICALLY WITH RESPECT TO THE VAX DIVERSION CASE, MRI FIRST CAME TO THE GOVERNMENT'S ATTENTION IN MARCH 1980, WHEN A U.S. FIRM APPLIED FOR AN EXPORT LICENSE TO SHIP AN ION IMPLANTATION SYSTEM TO MRI. COMMERCE'S COMPLIANCE DIVISION APPROPRIATELY REQUESTED A ROUTINE PRE-LICENSE CHECK OF MRI BY THE U.S. CONSULATE, CAPE TOWN (CONGEN). ON MAY 12, 1980, THE CONGEN REPORTED THAT MRI WAS A SUITABLE RECIPIENT OF U.S.-ORIGIN HIGH TECHNOLOGY. CONGEN BASED ITS RECOMMENDATION ON AN INTERVIEW WITH MRI'S DIRECTOR, DR. ATHOL M. HARRISON, AND ON A FAVORABLE WORLD TRADERS DATA REPORT (SIMILAR TO DUN AND BRADSTREET).

SUBSEQUENTLY, ON MAY 16, 1980, COMMERCE, DEFENSE AND TREASURY ALL WERE GIVEN HIGHLY SENSITIVE INFORMATION REQUIRING SPECIAL HANDLING INDICATING THAT SEMITRONIC AG (A FIRM KNOWN TO BE OWNED BY THE DIVERTER, RICHARD MUELLER) SWITZERLAND, WAS INTERESTED IN PURCHASING U.S.-ORIGIN SEMICONDUCTOR MANUFACTURING SYSTEMS THROUGH MRI FOR EVENTUAL RESALE, POSSIBLY TO THE USSR.

THE NOTATIONS MADE BY THE COMPLIANCE DIVISION AGENT WITH ACCESS TO THIS INFORMATION WERE INTERPRETED TO INDICATE MRI WAS THE COMPANY DIVULGING THE INFORMATION, AND, CONSEQUENTLY, THE LEAD WAS NOT GIVEN PRIORITY ATTENTION. IN ADDITION, THIS AGENT WAS D TAILED TO THE STATE DEPARTMENT FOR A YEAR AND NOT AVAILABLE TO FOLLOW UP WITHIN THE COMPLIANCE DIVISION ON THE PROCESSING OF THIS LEAD. SIMILAR HIGHLY SENSITIVE INFORMATION WAS PROVIDED TO COMMERCE ON APRIL 23, JUNE 26 AND JULY 21, 1980, BUT WERE NOT CONVEYED TO THE COMPLIANCE DIVISION.

AFTER RECEIPT OF THE MAY 16, 1980 INFORMATION, THE COMPLIANCE DIVISION REQUESTED TWO POST-SHIPMENT CHECKS BY CONGEN, AND REVIEWED COMMERCE LICENSING DATA ON MRI. ON NOVEMBER 17, 1981 AND FEBRUARY 25, 1982, CONGEN REPORTED FAVORABLY ON MRI, AN ON-SITE VISIT HAVING BEEN MADE BY A CONGEN OFFICIAL. THE CONGEN REPORTS, THEREFORE, DID NOT CORROBORATE THE NEGATIVE INFORMATION WE RECEIVED ON MAY 16TH.

LET ME STRESS THAT THE CONGEN NEVER CONVEYED ANY UNFAVORABLE INFORMATION TO US REGARDING MRI, NOR DID THEY EVER REPORT ANY CONNECTION BETWEEN MRI AND RICHARD MUELLER. IN FACT, BETWEEN APRIL 1980 AND MAY 1983, CONGEN REPEATEDLY REPORTED TO US THAT MRI AND DR. HARRISON WERE RELIABLE RECIPIENTS OF U.S. TECHNOLOGY AND RECOMMENDED ISSUANCE OF EXPORT LICENSES.

FOR EXAMPLE, IN A CABLE DATED SEPTEMBER 23, 1982, CONGEN RESPONDED TO ONE OF OUR PRE-LICENSE CHECK REQUESTS STATING THAT "CONSULATE GENERAL HAS KNOWN DR. HARRISON AND HIS INSTITUTE FOR SEVERAL YEARS AND CONSIDERS THEM RELIABLE RECIPIENTS OF SENSITIVE U.S. EQUIPMENT. THEREFORE RECOMMEND ISSUANCE OF LICENSE." INDEED, AS RECENTLY AS MAY 26, 1983, CONGEN RESPONDED FAVORABLY TO ANOTHER MRI PRE-LICENSE CHECK REQUEST STATING "POST HAS HAD NUMEROUS CONTACTS WITH DR. HARRISON IN THE PAST FEW YEARS ... AND WE CONSIDER HIS FIRM A RELIABLE TRADING PARTNER FOR U.S. FIRMS."

THESE FAVORABLE REPORTS SERVED TO MINIMIZE THE IMPORTANCE OF OTHER INFORMATION WE RECEIVED, SUCH AS A NOVEMBER 29, 1982, LETTER FROM A U.S. FIRM REPORTING MRI'S FAILURE TO REQUEST INSTALLATION SERVICES. LET ME CLARIFY, MR. CHAIRMAN, THAT THE U.S. COMPANY'S LETTER MADE NO ALLEGATIONS AGAINST MRI. RATHER, THE FIRM INFORMED US THAT, ALTHOUGH THE PRICE OF THE PHOTOMASK INSPECTION SYSTEM IT HAD SOLD TO MRI INCLUDED THE COST OF INSTALLATION, MRI HAD NOT REQUESTED INSTALLATION SERVICES.

AT THE SAME TIME, THE FIRM CITED ANOTHER FACTOR WHICH LESSENED THE UNUSUALNESS OF THIS CIRCUMSTANCE: SPECIFICALLY, THAT AN ENGINEER FROM MRI HAD BEEN TRAINED AT THE U.S. FIRM'S FACILITY AND WAS GENERALLY ATTESTED BY THAT FIRM'S FIELD SERVICE TRAINING PERSONNEL AS BEING THE SHARPEST ENGINEER THAT HAD EVER BEEN IN ONE OF THEIR TRAINING CLASSES. THEREFORE, IN THE U.S. FIRM'S OPINION, IT WOULD BE POSSIBLE FOR THIS PARTICULAR ENGINEER TO INSTALL, SET UP AND MAINTAIN THE U.S. EQUIPMENT BY HIMSELF. THE U.S. FIRM WENT ON TO SAY THAT THAT APPEARS TO BE WHAT HAD HAPPENED, JUDGING FROM MRI'S TELEXES.

OTHER INFORMATION WE RECEIVED ALSO CONTRIBUTED TO MRI'S APPEARANCE OF LEGITIMACY. FOR EXAMPLE, IN MAY 1983 OEE RECEIVED INFORMATION FROM ANOTHER U.S. FIRM THAT IN APRIL 1983, ONE OF THEIR TECHNICIANS HAD VISITED MRI AND REPORTED THAT MRI HAD SPECIAL CLEAN ROOMS FOR THE EQUIPMENT IT HAD PURCHASED FROM THE U.S. FIRM,

THAT ADDITIONAL CLEAN ROOMS WERE BEING PREPARED AS WELL AS OTHER PREPARATIONS, AND THAT THE TECHNICIAN HAD SEEN A "HUGE DIGITAL EQUIPMENT COMPUTER" BEING USED BY MRI TO MANUFACTURE INTEGRATED CIRCUITS.

THE IMPORTANCE OF REALIZING MISTAKES, MR. CHAIRMAN, IS TO EFFECTUATE SOLUTIONS SO THAT SIMILAR MISTAKES DON'T HAPPEN AGAIN. WHAT, THEN, IS COMMERCE DOING TO ENSURE THAT THE MISTAKES MADE IN THE MRI CASE DON'T OCCUR IN THE FUTURE?

FIRST, INSTEAD OF HAVING JUST ONE PERSON LOOKING AT HIGHLY CLASSIFIED INTELLIGENCE INFORMATION AND REPORTING BACK TO THE DIRECTOR OF THE ENFORCEMENT OFFICE, AS HAD BEEN THE PREVIOUS PRACTICE, SEVERAL SENIOR OPERATIONS AND PROGRAM SUPERVISORS IN OEE NOW EXAMINE SUCH INFORMATION. WE BELIEVE THIS SYSTEMATIC REVIEW OF INTELLIGENCE WILL MINIMIZE THE CHANCES OF IMPORTANT INFORMATION BEING OVERLOOKED. A BROADER REVIEW MECHANISM ALSO ENHANCES THE LIKELIHOOD THAT INFORMATION IMPORTANT TO TECHNOLOGY TRANSFER CONCERNS ARE RECOGNIZED AND SINGLED OUT FOR INVESTIGATION OR OTHER APPROPRIATE ENFORCEMENT AND LICENSING ACTION.

SECONDLY, COMMERCE'S OFFICE OF INTELLIGENCE LIAISON HAS BEEN CONSIDERABLY EXPANDED. TWO INDIVIDUALS FROM THE LIAISON OFFICE ARE ASSIGNED FULL-TIME TO EXPORT CONTROL MATTERS, THUS PREVENTING A RE-OCCURRENCE OF THE 1980 INCIDENTS WHEN NEGATIVE INFORMATION CONCERNING MRI WAS NOT PASSED ON TO COMMERCE'S ENFORCEMENT ARM.

THIRD, WE HAVE SENT TO ALL U.S. FOREIGN POSTS SPECIFIC INSTRUCTIONS ON THE CONDUCT ON PRE-LICENSE AND POST-SHIPMENT CHECKS. THIS GUIDANCE WILL HELP THE FOREIGN POST OFFICERS TO BETTER DO THEIR JOB BY SHOWING THEM WHAT TO LOOK FOR, AND WHAT TYPE OF INFORMATION SHOULD BE COMMUNICATED TO COMMERCE'S ENFORCEMENT OFFICE TO ENABLE THAT OFFICE TO MAKE BETTER ASSESSMENTS OF THE LEGITIMACY OF PROPOSED EXPORT TRANSACTIONS.

FINALLY, ALL CASES ARE PUT INTO THE NAME DATA FILES. IN FACT, THE CHIEF OF THE INTELLIGENCE DIVISION, WHO ADMINISTRATIVELY REFERS CASES FOR INVESTIGATION, ALSO HAS THE CASES AUTOMATICALLY ADDED TO THE COMPUTERIZED LICENSING SCREEN. HAVING ONE CENTRAL OFFICE RESPONSIBLE FOR ADDING NAMES TO THE SCREEN, RATHER THAN SPREADING THAT RESPONSIBILITY AROUND, MINIMIZES THE RISK THAT SOMEONE WILL FORGET TO ADD A NAME. SCREENING IS NOW AN INTEGRAL PART OF THE INVESTIGATION ASSIGNMENT AND INTELLIGENCE REVIEW PROCESS.

I WOULD LIKE TO POINT OUT THAT IN THE SPIRIT OF COOPERATION, AND IN THE COMMON INTEREST OF U.S. NATIONAL SECURITY, COMMERCE RESPONDED EXPEDITIOUSLY TO ALL REQUESTS MADE TO US BY CUSTOMS DURING THE COURSE OF THEIR INDEPENDENT INVESTIGATION INTO MRI. THIS WAS AN ONGOING PROCESS, STARTING FROM NOVEMBER 1983, WITH COMMERCE PROVIDING WHATEVER INFORMATION CUSTOMS REQUESTED, AS IT WAS REQUESTED. IN THE INTEREST OF A COMPREHENSIVE, COHESIVE U.S.

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EXPORT CONTROL/ENFORCEMENT PROGRAM, COMMERCE INTENDS TO CONTINUE TO PROVIDE CUSTOMS, AND OTHER PERTINENT AGENCIES, INFORMATION REQUESTED IN SUPPORT OF U.S. EFFORTS TO STEM ILLEGAL TECHNOLOGY TRANSFER.

MR. CHAIRMAN, GIVEN THE CONSTRAINTS OF AN OPEN SESSION, I HAVE TRIED TO BE AS FORTHRIGHT AS POSSIBLE REGARDING THE MRI CASE AND TO CONVEY TO YOU THE FACT THAT THE COMMERCE DEPARTMENT'S ENFORCEMENT PROGRAM HAS IMPROVED CONSIDERABLY IN THE LAST TWO YEARS AND WILL BE IMPROVING EVEN MORE IN THE NEAR FUTURE. COMMERCE FEELS STRONGLY THAT WE CAN MORE THAN FULFILL THE CONFIDENCE OF THE PRESIDENT IN HIS DECISION OF TWO WEEKS AGO, WHEN HE STATED THAT THE COMMERCE DEPARTMENT AND THE CUSTOMS SERVICE TOGETHER DO, INDEED, BRING IMPORTANT COMPLEMENTARY ASSETS TO THE ENFORCEMENT OF THE EXPORT ADMINISTRATION ACT.

THANK YOU.

The CHAIRMAN. Mr. Bryen.

STATEMENT OF STEPHEN D. BRYEN, DEPUTY ASSISTANT SECRETARY OF DEFENSE, INTERNATIONAL ECONOMIC, TRADE AND SECURITY POLICY

Dr. BRYEN. Thank you, Mr. Chairman. I regret being slightly delayed in getting here this morning.

THE ATTEMPTED DIVERSION OF THE VAX 11/782

Mr. Chairman, I appear before you today to discuss the attempted diversion to the Soviet Union of the VAX 11/782 computer system.

While it's not part of my statement, I would like to say at the beginning that we became involved in this case after the U.S. Customs officials telephoned us to tell us that they had made the first major seizure in cooperation with the German Government. We transported the equipment back to the United States from Germany. We were further involved in working out some of the efforts that were undertaken to retrieve the equipment that went on to Sweden.

I wish praise for the work of the U.S. Customs Service in this whole matter. It was a close call, as you well know. I believe we had some 7 minutes in West Germany to retrieve equipment after a court decision was made, actually an appeals court decision, which highlights another problem in the international cooperation area that I hope at some point we can make more progress on in terms of making more efficient the way we work with our allies abroad to prevent diversions.

I believe we have to, in this case, thank the Governments of West Germany and Sweden for their overall cooperation, assistance, and understanding of the problem we had.

The VAX computer case represents the largest single documented diversion attempt of its kind involving militarily sensitive equipment. It underscores the necessity of maintaining national security controls on free world trade. This necessity was recognized by the President in his recent decisions to strengthen the enforcement and license review mechanisms which implement U.S. export control laws.

Mr. Chairman, I know you'll ask me about this later on anyway—I can feel it coming—but we have believed since we have been in office that section 10(g) of the Export Administration Act of 1979 gave to the Defense Department and specifically to the Secretary of Defense sufficient authority to be involved in reviewing the type of export and the ultimate destination in this case. The problem, as you know, was that we weren't involved.

The CHAIRMAN. Let me just say, Dr. Bryen, that that was the intent of that act. There is no doubt about it in my mind and in the minds of others who were involved, certainly including Senator Jackson who had a part in it—that was the intent of that law. That's why we will get into this in more detail, but what we are trying to do in the extension of the Export Administration Act is clarify and make certain the language indicates what our intent was originally. I can't find anybody here on the Hill who partici-

pated in it who feels any differently than what you have just stated was the intent of that act at the time.

Dr. BRYEN. Mr. Chairman, the equipment brought back to America was state-of-the-art computer hardware which would have supported and accelerated Soviet military modernization programs. Senator Proxmire has already raised this important point in his opening statement. Had the Soviets received this material, they would have been able to produce vastly more accurate and destructive weapons systems. We believe they would have done so much sooner than they would otherwise.

The computer system had a complete configuration identical to a number of highly classified U.S. defense systems. We can brief the committee separately on that in closed session, but there are some applications that have been discussed today and I have with me an expert from the U.S. Army who is available to this committee today as well, if required.

Among the tasks that this particular system could carry out include the simulation of the operation of military systems, such as missile targeting, at faster than real-time, or the time it takes for a missile to hit its target; the simulation of terrain-following radar for cruise missiles and flight paths of intercontinental ballistic missiles; and command and control for targeting antiaircraft batteries of guns and missiles; and the design and manufacture of very high-speed integrated circuits. This application, essential for the manufacture of smart weapons, is totally embargoed to the Soviet Union and Eastern Europe.

The last item, the design and manufacture of sophisticated integrated circuits, is an item that has dominated our concerns in the Defense Department for the past 3 years. If I may divert a little bit from our statement, during the 1970's, the Soviets were able to acquire from the United States primarily, sometimes through conduits in West Europe and from some of the other Western European countries, the manufacturing capability to produce integrated circuits. In 1970, there were no integrated circuits in the Soviet weapons systems. In fact, they were using primarily vacuum tubes.

SOVIETS COPY INTEGRATED CIRCUITS FOR THEIR WEAPON SYSTEMS

In 1980, that situation had been stood on its head and the integrated circuits that are in Soviet weapon systems are exact copies of integrated circuits in this country.

We would not like to see clearly greater sophistication in terms of the type of circuitry available to the Soviet Union. In fact, we are right now attempting to upgrade our own weapons systems. We have a very important program funded by the Congress called the very high-speed integrated circuit program. We won't have that new technology in our weapons systems until the late 1980's at the earliest.

The commodities seized by the U.S. Customs Service in cooperation with West Germany and Sweden happened to represent less than half—that we know of—less than half of the sensitive commodities of this particular illegal shipment. Records show in all, some 15 containers were shipped. I believe we received back 7 of the 15. Now that in itself may not be conclusive. Some of the equip-

ment mixed in came under validated licenses and some of it under distribution licenses. I suspect some of it was sent under no license at all. Not all of the seized equipment is American. So it's not easy to reconstruct exactly what all of this amounts to. To a certain extent, we have to go through and puzzle together from what we've been able to obtain what the meaning of the shipment is.

If, as we understand, quite a bit of semiconductor equipment was mixed in and was lost to us, then we might conclude that the Soviets could have gained some 5 years in terms of research and other savings in resource and development in computer technology, data communication and computer software and, as I said before, integrated circuit technology.

This particular case is symptomatic of the problem that runs through CoCom and non-CoCom countries alike. I wouldn't attempt to differentiate—and I don't think the Soviets do—where they attempt to divert from. They look for a soft target and make use of it, whether it's France, England, the United States, South Africa, or Thailand, or wherever. They have maximum flexibility. They don't distinguish between legal and illegal and they don't worry about that. They worry about how to get it back to the Soviet Union for their military programs.

So we have been concerned in the Defense Department to have as much involvement overall in this process as we can get because through the expertise that resides in the Defense Department and the kind of problem-solving attitude we hope to be able to lend assistance to the other agencies involved in the enforcement, licensing and so on.

In the case of the VAX, my staff tells me there are some six free world countries that served as unwitting conduits to launder the VAX computer system. Richard Mueller, who was the mastermind of this particular diversion, established more than 60 front companies—that's quite a lot of front companies—in a number of free world countries to obtain militarily critical commodities. We are probably looking at the tip of the iceberg in this particular case and in other cases like it.

We have said for the past 3 years that the cornerstone of our defense system is a strong, qualitatively superior technological edge over the Soviets. Obviously, the illegal exports save the Soviets billions of dollars a year in research and development. We have attempted, Mr. Chairman, to assess the cost of this particular case and we have a pilot study underway at the moment to make an assessment that covers all goods in 1 year to see what this really means.

In this case, our estimate is that the Soviets will realize a savings of about $80 million a year for the next decade. It's $80 million each year for the next decade that they received for all the equipment, to give you some idea of the impact. That's the defense impact. We would like at a later time to present the entire study to your committee to give you a look at it. We would appreciate criticism of it. This is a terribly difficult area to assess the full damage. We are trying the study to get an idea how badly we have been hurt and to know what to emphasize in the future so we can prevent being hurt, which is equally important.

Mr. Chairman, the President's decision which affects both the Defense Department, the Customs Service, and the Department of Commerce, we think, is a very good and important decision. We are prepared to support it fully. We think, especially in this early stage where the Defense Department would be involved in the so-called West-West relations, we have to, to some extent, learn our way and organize ourselves for it. It's not traditional for the Defense Department to review West-West cases. While we have been involved to a certain extent in advising the Customs Service from time to time, most recently we were involved a few weeks ago in halting the export of chemicals that might have been used for manufacturing muscle gas. The chemicals were seized by the Customs Service. We still need to discern how best to use the resources that we have. We're working hard on that and we expect in the very near future as a result of the President's decision to be far more actively involved.

In the past 3 years, to the extent that we have been able to, by reading intelligence reports, by staying plugged into the system as best we could, we tried to do our bit. We have had some impact. We noticed that more than 2 years ago that the VAX was a target and called that to the attention of the Commerce Department and asked them to look for it to keep an eye out for it, and there were other items that we have pointed out. We've got an interagency task force on one item on which I'd rather brief the committee separately on privately that's turned out to be quite successful. But we think the President's decision will be very helpful and we look forward to the months ahead to see to it that it works.

That concludes my statement, Mr. Chairman.

The CHAIRMAN. Thank you, Dr. Bryen.

[The complete statement follows:]

STATEMENT OF DR. STEPHEN D. BRYEN, DEPUTY ASSISTANT SECRETARY OF DEFENSE, INTERNATIONAL ECONOMIC, TRADE AND SECURITY POLICY

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE.

MY NAME IS STEPHEN D. BRYEN. I AM THE DEPUTY ASSISTANT SECRETARY OF DEFENSE FOR INTERNATIONAL ECONOMIC, TRADE AND SECURITY POLICY.

I AM PLEASED TO APPEAR BEFORE YOU TODAY TO DISCUSS THE ATTEMPTED DIVERSION TO THE SOVIET UNION OF THE VAX 11/782 COMPUTER SYSTESM.

AT THE OUTSET, I WANT TO PRAISE THE OUTSTANDING WORK OF THE U.S. CUSTOMS SERVICE, PARTICULARLY OPERATION EXODUS, IN STOPPING THIS ILLEGAL SHIPMENT. I ALSO WANT TO EXTEND OUR GRATITUDE TO THE GOVERNMENTS OF WEST GERMANY AND SWEDEN FOR THEIR COOPERATION IN THIS MATTER.

THE VAX COMPUTER CASE REPRESENTS THE SINGLE LARGEST ATTEMPTED DIVERSION TO DATE OF MILITARILY SENSITIVE EQUIPMENT. IT UNDERSCORES THE NECESSITY OF MAINTAINING NATIONAL SECURITY CONTROLS ON FREE WORLD TRADE. THIS NECESSITY WAS RECOGNIZED BY THE PRESIDENT IN HIS RECENT DECISIONS TO STRENGTHEN THE ENFORCEMENT AND LICENSE REVIEW MECHANISMS WHICH IMPLEMENT U.S. EXPORT CONTROL LAWS.

THE EQUIPMENT BROUGHT BACK TO AMERICA WAS STATE-OF-THE-ART COMPUTER HARDWARE WHICH WOULD HAVE SUPPORTED AND ACCELERATED

SOVIET MILITARY MODERNIZATION PROGRAMS. HAD THE SOVIETS RECEIVED THIS MATERIAL, THEY WOULD HAVE BEEN ABLE TO PRODUCE VASTLY MORE ACCURATE AND DESTRUCTIVE WEAPONS.

IN FACT, THIS COMPUTER SYSTEM HAD A CONFIGURATION IDENTICAL TO A NUMBER OF HIGHLY CLASSIFIED U.S. DEFENSE SYSTSEMS. THERE ALSO ARE APPLICATIONS WE CAN TALK ABOUT. THEY INCLUDE:

- SIMULATION OF THE OPERATION OF MILITARY SYSTEMS, SUCH AS MISSILE TARGETING, AT FASTER THAN REAL-TIME, OR THE TIME IT TAKES FOR A MISSILE TO HIT ITS TARGET.

- SIMULATION OF TERRAIN-FOLLOWING RADAR FOR CRUISE MISSILES AND FLIGHT PATHS OF INTERCONTINENTAL BALLISTIC MISSILES.

- COMMAND AND CONTROL FOR TARGETING ANTI-AIRCRAFT BATTERIES OF GUNS AND MISSILES, AND

- THE DESIGN AND MANUFACTURE OF VERY HIGH SPEED INTEGRATED CIRCUITS. THIS APPLICATION, ESSENTIAL FOR THE MANUFACTURE OF "SMART WEAPONS," IS TOTALLY EMBARGOED TO THE SOVIET UNION AND EASTERN EUROPE.

THE COMMODITIES SEIZED REPRESENTED LESS THAN HALF OF THE HIGHLY SENSITIVE COMMODITIES OF THE ENTIRE ILLEGAL SHIPMENT. RECORDS SHOW THAT 15 CONTAINERS IN ALL WERE SHIPPED. SEVEN CONTAINERS SHIPPED WERE SEIZED BETWEEN SWEDEN AND WEST GERMANY. WE NOW HAVE CONCLUDED THAT ANOTHER EIGHT CONTAINERS OF SENSITIVE COMMODITIES MAY HAVE REACHED THE SOVIET UNION. IF SO, THE SOVIETS MAY HAVE GAINED FIVE YEARS IN TERMS OF RESEARCH AND OTHER SAVINGS IN RESOURCE DEVELOPMENT IN COMPUTER TECHNOLOGY, DATA COMMUNICATION, COMPUTER SOFTWARE AND INTEGRATED CIRCUIT TECHNOLOGY.

THIS ONE CASE IS A SYMPTON OF THE PROBLEM OF DIVERSION THROUGH COCOM AND NON-COCOM COUNTRIES ALIKE. DEFENSE CRITICS CLAIM THE PROBLEM OF DIVERSION IS NOT IN FREE WORLD TRADE. THEY CONTEND IT IS IN OUR WEST-TO-EAST TRADE TRANSACTIONS. OUR VALIDATED LICENSING SYSTEM IN WEST-TO-EAST TRADE, HOWEVER, HAS PROVEN SUCCESSFUL. IT HAS BEEN PROVEN SO SUCCESSFUL THAT THE SOVIETS ARE RESORTING TO FREE WORLD OUTLETS FOR THE SENSITIVE EQUIPMENT THEY REQUIRE TO UPGRADE THEIR MILITARY.

TO ILLUSTRATE THE POSSIBLE DIVERSIONS OF THIS PROBLEM, UP TO SIX FREE WORLD COUNTRIES SERVED AS UNWITTING CONDUITS TO LAUNDER THE VAX COMPUTER SYSTEM. RICHARD MUELLER, MASTERMIND OF THIS DIVERSION, ESTABLISHED MORE THAN SIXTY

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FRONT COMPANIES IN A NUMBER OF FREE WORLD COUNTRIES TO OBTAIN MILITARILY CRITICAL COMMODITIES. IN VIEW OF THE VAX CASE, WE ARE DEEPLY CONCERNED ABOUT WHAT OTHER SENSITIVE TECHNOLOGIES AND COMMODITIES WERE DIVERTED ILLEGALLY THROUGH THESE COMPANIES. WHILE WE CANNOT GAUGE HOW MANY OTHER PEOPLE MAY BE DOING THE SAME THING, INCREASING INFORMATION LEADS US TO BELIEVE THAT THE MAGNITUDE OF THE FREE WORLD DIVERSION PROBLEM IS HIGHLY SIGNIFICANT.

MR. CHAIRMAN, THE CORNERSTONE OF OUR DEFENSE SYSTEM IS A STRONG, QUALITATIVE TECHNOLOGICAL EDGE TO OFFSET THE SOVIET BLOC'S QUANTITATIVE ADVANTAGES. SUCCESSFUL ILLEGAL EXPORTS COULD BE SAVING THE SOVIETS MORE THAN A BILLION DOLLARS A YEAR IN RESEARCH AND DEVELOPMENT, NOT TO MENTION HUNDREDS OF THOUSANDS OF MAN HOURS. THOSE COSTS ARE BORNE DIRECTLY BY THE U.S. TAXPAYER. A LITTLE LESS THAN HALF OF THE ENTIRE DEFENSE BUDGET GOES FOR RESEARCH, DEVELOPMENT, AND ACQUISITION. CONSEQUENTLY, THE NEED TO MAINTAIN THE TECHNOLOGICAL LEAD WE LOSE TO THE SOVIET MILITARY THROUGH ILLEGAL DIVERSIONS HELPS KEEP DEFENSE COSTS HIGH.

THE PRESIDENT'S DECISION TO IMPROVE OUR MONITORING SYSTEM OVER THE FLOW OF HIGH TECHNOLOGY IS BASED ON THE FACT, HIGHLIGHTED IN THE VAX CASE, THAT COMMERCIAL TECHNOLOGY IS BEING

IMPROVED AT SUCH A RAPID PACE THAT ITS PERFORMANCE IN LITTLE TIME EXCEEDS THAT OF OUR OWN MILITARY SYSTEMS.

THE AIM OF DEFENSE DEPARTMENT REVIEW OF SELECTED VALIDATED LICENSE APPLICATIONS FOR EXPORTS TO CERTAIN FREE WORLD COUNTRIES WILL BE TO MAKE A NATIONAL SECURITY ASSESSMENT OF THE COMMODITY TO BE EXPORTED. IT ALSO WILL BE TO SUBJECT THE APPLICATION TO END-USER CHECKS. WE ARE SETTING UP AN ADP SYSTEM TO DO THIS.

THE PRESIDENT'S DECISION ALSO EXTENDS IN PRINCIPLE TO DEFENSE REVIEW OF DISTRIBUTION LICENSE APPLICATIONS. BECAUSE THERE IS LESS SCRUTINY OF EXPORTS UNDER DISTRIBUTION LICENSES, AND BECAUSE END-USERS UNDER THE DISTRIBUTION LICENSE SYSTEM TEND TO BE DEALERS OR MIDDLEMEN IN EUROPE OR IN OTHER FREE WORLD COUNTRIES, THIS SYSTEM IS AN UNFORTUNATE CONDUIT BY WHICH U.S. TECHNOLOGY CAN BE CARRIED TO THE EAST.

THE PRESIDENT'S DECISION TO PERMIT EXPANDED REVIEW OF LICENSES BY THE DEPARTMENT OF DEFENSE IS CONSISTENT WITH THE NEED TO PREVENT FUTURE SITUATIONS SUCH AS THE VAX CASE. NEVERTHELESS, THE ADMINISTRATION IS ALSO CONCERNED TO AVOID UNNECESSARY DELAYS OR DISRUPTION IN LEGITIMATE LICENSING. SOME HAVE EXPRESSED CONCERN THAT DOD REVIEW WILL UNDULY SLOW THE LICENSING. LET ME ASSURE YOU THAT THE NEW PROCEDURES

ARE EXPLICITLY DESIGNED TO PREVENT THIS. WHILE WE FEEL STRONGLY THAT EVERY EFFORT MUST BE MADE TO STOP EXPORTS WHICH WILL ENHANCE SOVIET DEFENSE CAPABILITY, WE ARE ALSO FULLY COMMITTED TO PROVIDING THE MOST EXPEDITIOUS DEFENSE DEPARTMENT ACTION ON THESE LICENSES THAT WE DO REVIEW.

THE PRESIDENT'S DECISION ALSO PARALLELS INCREASING CONGRESSIONAL CONCERN OVER THE PROBLEM OF FREE WORLD DIVERSIONS. THE DECISION NOT ONLY SETS AN EXAMPLE BUT BOLSTERS OUR EFFORTS IN COCOM AND WITH OTHER FRIENDLY, NON-ALLIED COUNTRIES TO STRENGTHEN MULTILATERAL CONTROLS AND ENFORCEMENT OVER STRATEGIC TRADE. WE BELIEVE THESE ARE ESSENTIAL STEPS TO STRENGTHEN THE CONTROLS OVER LOSS OF WESTERN TECHNOLOGY ESSENTIAL TO SECURITY INTERESTS OF THE UNITED STATES AND THE ALLIES.

THANK YOU, MR. CHAIRMAN. I WILL BE HAPPY TO ANSWER QUESTIONS OF THE COMMITTEE.

The CHAIRMAN. Mr. Rudman.

STATEMENT OF WILLIAM RUDMAN, DIRECTOR, STRATEGIC INVESTIGATIONS DIVISION, U.S. CUSTOMS SERVICE

Mr. RUDMAN. Thank you, Mr. Chairman. My name is William Rudman and I am accompanied by Roger Urbanski, Chief of our Technology Investigation Branch.

[The complete statement follows:]

STATEMENT OF WILLIAM RUDMAN
DIRECTOR, STRATEGIC INVESTIGATIONS DIVISION
U.S. CUSTOMS SERVICE
BEFORE THE UNITED STATES SENATE
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
APRIL 2, 1984

MR. CHAIRMAN AND DISTINGUISHED MEMBERS OF THIS COMMITTEE, IT IS INDEED A PLEASURE TO APPEAR BEFORE YOU TODAY TO DISCUSS CUSTOMS INVESTIGATION OF THE RICHARD MUELLER ORGANIZATION, WHICH IS GENERALLY KNOWN AS THE "VAX" CASE.

ON NOVEMBER 3, 1983, THE U.S. CUSTOMS ATTACHE, BONN, RECEIVED INFORMATION FROM A CONFIDENTIAL SOURCE THAT RICHARD MUELLER WAS IN THE PROCESS OF DIVERTING U.S. ORIGIN, STRATEGIC EQUIPMENT FROM SOUTH AFRICA TO THE SOVIET UNION. THE SOURCE ALLEGED THAT THE EQUIPMENT IN QUESTION WAS POSSIBLY MANUFACTURED BY THE DIGITAL EQUIPMENT CORPORATION (DEC). THE SOURCE PROVIDED A NUMBER WHICH WAS BELIEVED TO PROVIDE SOME IDENTIFICATION OF THE TRANSACTION ITSELF. FINALLY, THE CUSTOMS ATTACHE WAS TOLD THAT THE SUSPECT SHIPMENT WAS, AT THAT MOMENT, ON BOARD THE M/V ELGAREN ON THE HIGH SEAS IN THE AREA OF NORTHERN EUROPE.

LATER, ON NOVEMBER 3RD, THE CUSTOMS ATTACHE PROVIDED THE NUMBER GIVEN BY HIS SOURCE TO U.S. CUSTOMS SERVICE HEADQUARTERS, WASHINGTON, D.C. USING THIS NUMBER, CUSTOMS LEARNED FROM THE MANUFACTURER ON NOVEMBER 4TH THAT THE EQUIPMENT BEING DIVERTED WAS A DEC VAX 11/782 COMPUTER, ONE OF THE MOST ADVANCED COMPUTER SYSTEMS AVAILABLE. IT WAS ALSO LEARNED THAT DEC HAD SOLD THE VAX 11/782 TO A NEW YORK FIRM.

ADVISED OF THE SERIOUSNESS OF THIS DIVERSION AT THE SAME MOMENT AS THE INFORMATION WAS RECEIVED, THE U.S. CUSTOMS ATTACHE, BONN, IMMEDIATELY ENLISTED THE ASSISTANCE OF HIS COUNTERPART ATTACHES IN PARIS AND LONDON. AN ALL-OUT SEARCH FOR THE M/V ELGAREN WAS INITIATED. THE INITIAL GOAL OF CUSTOMS EFFORTS WAS TO STOP THE SHIPMENT FROM PROCEEDING.

ON NOVEMBER 8, 1983, THE U.S. CUSTOMS ATTACHE, PARIS, DISCOVERED THAT THE M/V ELGAREN HAD CALLED AT THE PORT OF ANTWERP, BELGIUM ON NOVEMBER 5TH. THE CUSTOMS ATTACHE WAS ABLE TO LOCATE AND EXAMINE THE MANIFEST FILED AT ANTWERP BY THE M/V ELGAREN. THE MANIFEST CONFIRMED THAT THERE WERE THREE CONTAINERS ON BOARD THE M/V ELGAREN BEING SHIPPED FROM CAPETOWN TO THE FIRM INTEGRATED TIME AG, IN CARE OF A FREIGHT FORWARDER IN SWEDEN. THE CUSTOMS ATTACHE, BONN, WAS ABLE TO DETERMINE THAT THE FIRM INTEGRATED TIME AG WAS, IN FACT, A FIRM OPERATED BY RICHARD MUELLER, A CUSTOMS FUGITIVE LONG KNOWN TO BE ENGAGED IN ILLEGAL U.S.-ORIGIN TECHNOLOGY TRANSFERS TO THE SOVIETS AND OTHER PROSCRIBED EAST BLOC DESTINATIONS.

THE CUSTOMS ATTACHE, PARIS, DETERMINED THAT THE M/V ELGAREN WOULD DISCHARGE THE INTEGRATED TIME AG MERCHANDISE AT THE PORT OF MALMO, SWEDEN, WITH AN INTERMEDIATE STOP AT THE PORT OF HAMBURG, WEST GERMANY.

BASED UPON PRIOR EXPERIENCE WITH THE WEST GERMAN GOVERNMENT IN SIMILAR MATTERS, THE CUSTOMS ATTACHE IMMEDIATELY MET WITH HIS COLLEAGUES IN THE GERMAN FINANCE AND JUSTICE MINISTRIES. SINCE THE M/V ELGAREN WOULD ONLY

TRANSIT HAMBURG AND NOT DISCHARGE THE INTEGRATED TIME AG CONTAINERS THERE, THE GERMAN GOVERNMENT DECIDED THAT THE U.S. DEPARTMENT OF JUSTICE HAD TO MAKE A FORMAL REQUEST FOR ASSISTANCE VIA THE GERMAN JUSTICE MINISTRY UNDER ESTABLISHED ARRANGEMENTS BETWEEN THE TWO NATIONS FOR THE RENDERING OF ASSISTANCE IN CRIMINAL MATTERS.

IN ORDER TO SATISFY THE REQUIREMENTS OF THE WEST GERMAN GOVERNMENT IN THIS MATTER, CUSTOMS CREATED A SPECIAL TASK GROUP. THE GROUP REQUESTED AN EMERGENCY MEETING ON NOVEMBER 8, 1983, WITH KEY DEPARTMENT OF JUSTICE PERSONNEL IN ORDER TO OBTAIN THE NECESSARY JUSTICE DEPARTMENT/MINISTRY OF JUSTICE MUTUAL ASSISTANCE. ALSO PARTICIPATING AT THE MEETING WERE OFFICIALS OF THE OFFICE OF EXPORT ENFORCEMENT, U.S. DEPARTMENT OF COMMERCE (OEE), WHO WERE INVITED AT THE REQUEST OF THE U.S. CUSTOMS SERVICE.

ALL INFORMATION AVAILABLE TO THE U.S. CUSTOMS SERVICE WAS SHARED WITH DOJ AND OEE. OEE ADVISED THAT THEY WERE AWARE THAT A VALIDATED EXPORT LICENSE HAD BEEN ISSUED TO THE NEW YORK FIRM TO EXPORT A VAX 11/782 TO A SOUTH AFRICAN FIRM CALLED MICROELECTRONICS RESEARCH INSTITUTE (PTY) LTD. (MRI). THEY ALSO ADVISED THAT MRI HAD NOT BEEN ISSUED A REEXPORT LICENSE TO SHIP THE VAX 11/782 OUT OF SOUTH AFRICA.

ON NOVEMBER 8, 1983, THE U.S. CUSTOMS SERVICE'S PRIMARY OBJECTIVE WAS TO DENY DELIVERY OF THE VAX 11/782 TO THE SOVIET UNION. IN ORDER TO ACCOMPLISH THIS OBJECTIVE, IT WAS NECESSARY TO SATISFY A WEST GERMAN COURT THAT A SOVIET END DESTINATION WAS INTENDED. DURING THE EVENING OF

NOVEMBER 8, 1983, A FORMAL REQUEST FOR ASSISTANCE WAS TRANSMITTED TO THE GERMAN MINISTRY OF JUSTICE BY THE U.S. DEPARTMENT OF JUSTICE. IT CONTAINED THE PROBABLE CAUSE SUPPORTING THE RUSSIAN DIVERSION THAT WAS AVAILABLE TO THE U.S. CUSTOMS SERVICE AND THE DOJ. THIS FORMAL REQUEST, RECEIVED IN WEST GERMANY ON NOVEMBER 9TH, FORMED THE LEGAL BASIS FOR THE SUBSEQUENT ENFORCEMENT ACTIVITY.

IT WAS LEARNED THAT THE M/V ELGAREN WOULD ARRIVE HAMBURG, ON NOVEMBER 9, 1983, AND WAS SCHEDULED TO DEPART THAT CITY ON THE SAME DAY. THE CUSTOMS ATTACHE, BONN, ACCOMPANIED GERMAN CUSTOMS OFFICIALS TO PRESENT THE HAMBURG STATE ATTORNEY WITH THE U.S. REQUEST FOR ASSISTANCE. AN AFFIDAVIT WAS PREPARED BY THE STATE ATTORNEY TO PETITION THE COURT TO ISSUE A SEARCH AND SEIZURE WARRANT FOR THE SUSPECT SHIPMENT ON BOARD THE M/V ELGAREN.

A WARRANT WAS ISSUED SEVEN MINUTES PRIOR TO THE SAILING, AND THE WEST GERMAN CUSTOMS SERVICE BOARDED THE M/V ELGAREN AND SEIZED THE THREE INTEGRATED TIME AG CONTAINERS. FOUND WITHIN THE CONTAINERS WERE SIGNIFICANT QUANTITIES OF STRATEGIC COMMODITIES IN ADDITION TO THE VAX 11/782 COMPUTER SYSTEM.

THE SPECIAL AGENT IN CHARGE, JFK AIRPORT, NEW YORK, APPLIED FOR A SEARCH WARRANT FOR THE BUSINESS RECORDS OF THE NEW YORK FIRM, WHICH HAD EXPORTED THE VAX 11/782 TO MRI. THE WARRANT WAS EXECUTED ON NOVEMBER 10, 1983. PERTINENT RECORDS WERE SEIZED AND ARE PRESENTLY BEING PREPARED FOR PRESENTATION TO A GRAND JURY.

DUE TO THE URGENCY OF THE SITUATION AND THE CONCERN THAT SOUTH AFRICAN CONSPIRATORS MIGHT DESTROY EVIDENCE, CUSTOMS AND DOJ VISITED THE EMBASSY OF SOUTH AFRICA ON NOVEMBER 10, 1983. THE SOUTH AFRICAN GOVERNMENT OFFICIALLY INVITED CUSTOMS TO INVESTIGATE THE MUELLER SHIPMENT(S) IN THAT COUNTRY. THE JOINT U.S. CUSTOMS/SOUTH AFRICAN INVESTIGATION DEVELOPED THE FOLLOWING INFORMATION:

RICHARD MUELLER HAD ESTABLISHED A SERIES OF SOUTH AFRICAN HOLDING COMPANIES THROUGH TWO SWISS BASED FIRMS; DAN CONTROL AG AND SEMITRONIC AG. THROUGH THESE SWISS FIRMS, MUELLER CONTROLLED SIX SOUTH AFRICAN COMPANIES INCLUDING MRI, THE APPROVED SOUTH AFRICAN END-USER ON SIXTEEN DOC LICENSES VALUED AT MORE THAN $7 MILLION.

THE MUELLER CONTROLLED SOUTH AFRICAN COMPANIES DIVERTED 15 CONTAINERS OF CRITICAL U.S. ORIGIN COMMODITIES FROM SOUTH AFRICA TO EUROPE DURING 1983. THESE INCLUDED THE 3 CONTAINERS SEIZED IN HAMBURG (AND 4 CONTAINERS SUBSEQUENTLY DETAINED ON NOVEMBER 15, 1983, IN SWEDEN AND LATER SEIZED). THE OTHER 8 CONTAINERS WERE DIVERTED VIA SWEDEN DURING THE FIRST HALF OF 1983 AND PRIOR TO THE INVOLVEMENT OF THE U.S. CUSTOMS SERVICE IN THIS MATTER.

EVIDENCE OF ISOLATED AIR SHIPMENTS HAS ALSO BEEN FOUND BY THE SOUTH AFRICANS. APPROPRIATE LEADS ARE BEING PURSUED BY THE U.S. CUSTOMS SERVICE.

THE SOUTH AFRICANS ALSO DETAINED 7 ADDITIONAL SEALED, UNMARKED SHIPPING CARTONS. THEY WERE FOUND ON THE PREMISES OF NRI, CAPETOWN, ALONG WITH A GUTTED VAX 11/780 COMPUTER SYSTEM AND OTHER DEC HARDWARE. THIS IS ALL THAT REMAINS OF THE MORE THAN $7 MILLION WORTH OF CRITICAL TECHNOLOGY APPROVED FOR EXPORT FROM THE UNITED STATES BY COMMERCE TO NRI SINCE 1980.

ON NOVEMBER 15, 1983, (AND BASED UPON INFORMATION WHICH THEY HAD RECEIVED FROM U.S. CUSTOMS) THE SWEDISH CUSTOMS SERVICE DISCOVERED 4 ADDITIONAL CONTAINERS OF U.S. ORIGIN COMPUTER EQUIPMENT DIVERTED FROM SOUTH AFRICA AND DESTINED TO THE SOVIET UNION. THESE 4 CONTAINERS WERE ALSO UNDER THE CONTROL OF THE RICHARD MUELLER FRONT FIRM, INTERGRATED TIME AG.

ON NOVEMBER 24, 1983, THE SWEDISH CUSTOMS DISCOVERED ONE ADDITIONAL SHIPMENT WHICH HAD ARRIVED IN SWEDEN FROM SOUTH AFRICA. THIS SHIPMENT CONSISTED OF SOFTWARE WHICH WAS LINKED TO THE FIRST 4 CONTAINERS DETAINED BY THE SWEDES ON NOVEMBER 15, 1983.

THE MATERIALS WERE EXAMINED BY THE SWEDISH WAR MATERIEL INSPECTORATE WHICH AFTER A CAREFUL REVIEW RULED THAT THE EQUIPMENT WAS OF A MILITARY NATURE AND ORDERED IT TO BE SEIZED.

ON DECEMBER 16, 1983, THE EQUIPMENT SEIZED BY THE WEST GERMAN CUSTOMS SERVICE IN HAMBURG WAS TURNED OVER TO THE U.S. CUSTOMS SERVICE, TO BE USED

AS EVIDENCE IN UPCOMING CRIMINAL PROCEEDINGS IN THE UNITED STATES. THE EQUIPMENT WAS AIRLIFTED FROM WEST GERMANY WITH THE ASSISTANCE OF THE U.S. DEPARTMENT OF DEFENSE. IT IS PRESENTLY UNDER THE CUSTODY AND CONTROL OF THE U.S. CUSTOMS SERVICE IN NEW YORK.

ON JANUARY 14, 1984, THE EQUIPMENT SEIZED BY THE GOVERNMENT OF SWEDEN WAS TURNED OVER TO THE U.S. THE CARGO WAS SEIZED BY THE U.S. CUSTOMS SERVICE AND AIRLIFTED TO THE UNITED STATES WHERE IT ALSO WILL BE USED AS EVIDENCE IN UPCOMING CRIMINAL PROCEEDINGS. THE SWEDISH CARGO ARRIVED IN THE UNITED STATES ON JANUARY 15TH AND IS PRESENTLY UNDER THE CUSTODY AND CONTROL OF THE UNITED STATES CUSTOMS SERVICE IN VIRGINIA.

AS A RESULT OF THE DETENTION AND SEIZURES OF THE RICHARD MUELLER SHIPMENTS, AND DUE TO THEIR FREQUENT CONTACT WITH OUR ATTACHE IN BONN, THE GOVERNMENT OF SWEDEN INITIATED ITS OWN INVESTIGATION INTO THIS MATTER. THIS INVESTIGATION FOCUSED ON A SWEDISH BUSINESSMAN WHO APPEARED TO BE VERY PROMINENT IN THE MUELLER ORGANIZATION. NUMEROUS SEARCH WARRANTS WERE EXECUTED WHICH RESULTED IN THE SEIZURE OF COMPELLING EVIDENCE WHICH ESTABLISHED THAT THE BUSINESSMAN WAS A RICHARD MUELLER DEPUTY WHO HAS BEEN ASSOCIATED WITH HIM SINCE AT LEAST 1979. ON THE BASIS OF EVIDENCE OBTAINED, THE SWEDISH BUSINESSMAN WAS ARRESTED ON FEBRUARY 24, 1984, AND CHARGED WITH NUMEROUS VIOLATIONS OF SWEDISH LAW INCLUDING SMUGGLING, TAX AND FOREIGN EXCHANGE FRAUD. IF CONVICTED, HE FACES IMPRISONMENT OF UP TO 6 YEARS.

SINCE THIS INVESTIGATION WAS INITIATED, THE U.S. CUSTOMS SERVICE HAS BEEN ABLE TO LINK NUMEROUS OTHER KNOWN DIVERTERS TO MUELLER AND HIS SWEDISH BUSINESS PARTNER. AS AN EXAMPLE, IT HAS RECENTLY BEEN DISCOVERED THAT CUSTOMS FUGITIVE BRIAN MOLLER-BUTCHER HAS UTILIZED MUELLER'S SWEDISH PARTNER TO DIVERT STRATEGIC COMMODITIES TO THE EAST BLOC. IN ADDITION, AS A RESULT OF THE INTENSE INVESTIGATION INITIATED BY THE SWEDISH GOVERNMENT, A SHIPMENT OF U.S.-ORIGIN SEMICONDUCTOR MANUFACTURING EQUIPMENT WAS SEIZED ON JANUARY 24, 1984, AS IT WAS TRANSSITTING SWEDEN ENROUTE TO EAST GERMANY. THIS ILLEGAL DIVERSION HAS BEEN LINKED TO MOLLER-BUTCHER.

DUE TO THE STRATEGIC IMPORTANCE OF THE VAX 11/782 COMPUTER SYSTEM, U.S. CUSTOMS INITIATED A TRACE ON ALL SUCH SYSTEMS. THE MANUFACTURER PROVIDED A LIST WHICH IDENTIFIED ALL SALES OF VAX 11/782S. IN ALL, APPROXIMATELY 125 VAX 11/782S HAVE BEEN MARKETED INCLUDING THE SYSTEM WHICH WAS RECOVERED IN THE HAMBURG CONTAINER. THE CUSTOMS SERVICE HAS RECENTLY DEVELOPED RELIABLE INFORMATION THAT ONE OF THESE VAX 11/782 SYSTEMS WAS SUCCESSFULLY DIVERTED TO THE SOVIET UNION. IT HAS BEEN LEARNED THAT THE SYSTEM WAS EXPORTED TO WESTERN EUROPE AND SUBSEQUENTLY DIVERTED TO THE SOVIET UNION THROUGH THE MUELLER ORGANIZATION. AS THIS IS A MATTER STILL UNDER INVESTIGATION, NO FURTHER DETAILS MAY BE DISCLOSED AT THIS TIME.

DURING FEBRUARY AND MARCH OF 1984, A MULTI-AGENCY REVIEW PANEL EVALUATED THE COMPUTER EQUIPMENT RETURNED TO THE UNITED STATES BY SWEDISH AND WEST GERMAN AUTHORITIES, AS WELL AS THE SEMICONDUCTOR PRODUCTION EQUIPMENT LICENSED BY COMMERCE TO MRI. (THAT EQUIPMENT WAS SUCCESSFULLY DIVERTED

FROM SOUTH AFRICA PRIOR TO THE SWEDISH AND GERMAN SEIZURES). THE CONCLUSIONS REACHED BY THAT PANEL, INDICATED THAT THE MUELLER ORGANIZATION HAD SUCCESSFULLY DIVERTED EQUIPMENT WORTH MILLIONS OF DOLLARS WHICH HAS HAD AN ADVERSE IMPACT ON THE NATIONAL SECURITY OF THE UNITED STATES (DETAILS ARE CLASSIFIED).

AFTER THE EQUIPMENT WAS INVENTORIED BY CUSTOMS PERSONNEL, A SERIES OF UNDEVELOPED LEADS WERE PREPARED FOR DISSEMINATION TO CUSTOMS FIELD OFFICES AROUND THE WORLD. PRELIMINARY RESULTS FROM MANY OF THOSE FIELD OFFICES HAVE COME IN AND INDICATE THAT MUCH OF THE U.S.-PRODUCED EQUIPMENT ACQUIRED BY THE MUELLER ORGANIZATION WAS PURCHASED BY THEM IN EUROPE UNDER COMMERCE'S DISTRIBUTION LICENSE SYSTEM. THIS INCLUDES EQUIPMENT MANUFACTURED BY AT LEAST THREE PROMINENT U.S.-BASED FIRMS. THESE LEADS WILL BE EXPANDED IN ORDER TO ACCESS CRIMINAL CULPABILITY OF THESE FIRMS AS DOCUMENTATION ALREADY REVIEWED REFLECTS THAT THEY SOLD LICENSABLE EQUIPMENT TO MUELLER THROUGH HIS GERMAN AND SWISS SUBSIDIARIES LONG AFTER HE HAD BEEN PLACED ON DOC DENIAL LIST.

SINCE THE INITIATION OF THE INVESTIGATION, THE CUSTOMS SERVICE HAS WORKED CLOSELY WITH WEST GERMAN AUTHORITIES. THE WEST GERMAN STATE PROSECUTOR AND THE CUSTOMS INVESTIGATIONS OFFICE IN LUBECK HAVE BEEN CONDUCTING A FAR REACHING PROBE INTO ALL OF THE ACTIVITIES OF MUELLER AND HIS ASSOCIATES, INCLUDING CUSTOMS FUGITIVE VOLKER NAST, FORMER DEC EMPLOYEES MANFRED SCHROEDER AND NORBERT STOLTENBERG, MUELLER'S BROTHER-IN-LAW HARALD BICKENBACH AND FIVE OTHER WEST GERMAN NATIONALS. THE INVESTIGATIONS THERE ARE EXPECTED TO RESULT IN CHARGES OF BANKRUPTCY FRAUD, EXPORT VIOLATIONS AND TAX EVASION AGAINST THESE INDIVIDUALS.

A TEAM OF CUSTOMS SPECIAL AGENTS HAS RECENTLY RETURNED FROM LUBECK WHERE THEY REVIEWED MUCH OF THE MATERIAL OBTAINED BY THE WEST GERMANS IN THEIR CASE AGAINST THE MUELLER ORGANIZATION. IN ADDITION TO SUBSTANTIATION OF THE USAGE OF THE DISTRIBUTION LICENSE SYSTEM BY THE MUELLER GROUP TO OBTAIN SIGNIFICANT AMOUNTS OF U.S.-ORIGIN STRATEGIC TECHNOLOGY IN EUROPE, MATERIAL HELD BY THE WEST GERMANS REFLECTS THAT MUELLER, NASI, SCHROEDER AND OTHERS WERE FREQUENTLY IN THE SOVIET UNION INSTALLING U.S.-PRODUCED TECHNOLOGY THAT THEY DIVERTED FROM THE UNITED STATES. MUCH EVIDENCE EXISTS THERE WHICH SHOWS THAT MUELLER FUNNELED THIS EQUIPMENT THROUGH AN INTRICATE LABYRINTH OF SHELL COMPANIES FROM WEST TO EAST FOR YEARS AND FUNDED THIS ENTIRE MECHANISM THROUGH A SERIES OF SWISS HOLDING COMPANIES AND BANK ACCOUNTS.

IN CONCLUSION, I WOULD LIKE TO EMPHASIZE THAT THE INVESTIGATION IN WEST GERMANY, AS WELL AS THOSE IN THE UNITED STATES AND IN SWEDEN, ARE FAR FROM COMPLETE. WE ARE CONFIDENT, HOWEVER, THAT THIS SPIRIT OF INTERNATIONAL COOPERATION, UNPRECEDENTED IN THE AREA OF TECHNOLOGY TRANSFER INVESTIGATIONS, WILL CONTINUE AND THAT IT WILL RESULT IN THE CRIMINAL PROSECUTION OF BOTH THE COMPANIES AND INDIVIDUALS INVOLVED IN THESE DIVERSIONS IN THE UNITED STATES, WEST GERMANY AND SWEDEN. TO DATE THESE ENFORCEMENT ACTIONS INITIATED BY THE U.S. CUSTOMS SERVICE HAVE RESULTED IN THE EXPOSURE AND DISMEMBERMENT OF THE LARGEST DIVERSION ORGANIZATION IN HISTORY. WE EXPECT THAT THE INVESTIGATION WILL PROGRESS AND EXPOSE FURTHER LINKS BETWEEN MUELLER AND OTHER MAJOR DIVERTERS AND SEVER THESE LONG ESTABLISHED SOVIET TENTACLES.

MR. CHAIRMAN, THANK YOU FOR PERMITTING ME TO PRESENT THIS TESTIMONY, IN WHICH I HAVE PROVIDED THE COMMITTEE WITH A GENERAL OVERVIEW OF THE SUCCESSFUL INVESTIGATIVE METHODS USED BY THE U.S. CUSTOMS SERVICE IN COMBATTING ILLICIT U.S. TECHNOLOGY ACQUISITION BY THE SOVIET BLOC AND PROTECTING OUR NATIONAL SECURITY. IF YOU HAVE ANY QUESTIONS I WOULD BE PLEASED TO ANSWER THEM.

The CHAIRMAN. Thank you, Mr. Rudman.

Mr. Archey, as I listened to your testimony, it takes me back over several years. I don't mean just your testimony, but also Mr. Bryen's and Mr. Rudman's. Being an advocate of a strong national defense during all of my career in the Senate, it has been a great difficulty for me to understand the continual shipment by both legal and illegal means of high-technology equipment that aids and abets the Soviet Union. As a result, as has been stated many, many times, increases needed for our defense budget become a great political topic, particularly in a Presidential election year. I don't know how you exactly quantify how many billions of dollars have been wasted defending ourselves against our own technology, but it has been large amounts.

GOVERNMENT NEEDS TO LEARN BY PAST MISTAKES

The reason I say as I listened to your testimony, is that I have listened to people testify for 8 or 9 years now and the testimony is pretty much the same even though there have been different people, and three different administrations, two Republican and one Democratic. I would agree with you that in 1980 when you were at Customs that your statement about the whole Government—not just Commerce—not taking this seriously is absolutely correct. It has been kind of up and downhill, but generally I think your statement is correct. I would also agree with your statement that when we talk about the mistakes of Commerce that it's important in export control to realize your mistakes so that they don't happen again.

I've also heard that comment—and I don't mean to single you out personally and I'm not doing that—but I have heard that comment over, and over, and over again. But the mistakes continue. I don't question your sincerity. I don't question the sincerity of this Commerce Department or this administration. I didn't question the sincerity of the Carter administration. All of you want to stop it. But it doesn't stop.

I would also say that there has been improvement. Certainly the attitude of this administration compared to the Carter administration has been to do more. The intent is there. The sincerity is there and on a scale of 10 we were looking at 1 in performance and we are now at 2, maybe 3, still leaving a big gap. So there is improvement, yes.

Under Secretary Olmer testified on this and I agree with him. He's a dedicated individual and he's worked very hard at trying to solve this problem. But after watching it now for a long number of years and being very interested in it, I came to the conclusion that it isn't possible to solve. The interagency battles continue. The biases of Commerce, Defense, and State go on, regardless of who is the President or which party happens to occupy the White House. That's exactly why I came to the conclusion 2 or 3 years ago that there was only one way to solve the problem—create a separate Office of Strategic Trade. Your Department is charged—because of its very nature as the Commerce Department—to promote business. That's your function. Defense is supposed to defend the country. The State Department—I've never figured out what their function is.

But in any event, each has their own bias and the interagency, interdepartmental bickering goes on, maybe to a somewhat lesser extent, in this administration, but it's only relative and it's only marginal. I have been rebuffed at every turn on the Office of Strategic Trade. It isn't going to become law, not maybe even a study. Wait until we get to conference—that's likely to go if the House has its way. But the more I have listened this past year, the more convinced I have become that I was right. It's the only way you could eliminate the bias of Defense because if they had their way they wouldn't sell anything; everything would have military significance. If Commerce had their way, they would sell everything because it means some jobs. Again, State, I don't know what their bias is. It switches from time to time. But I still think that we are missing the boat, that we ought to have a separate Office of Strategic Trade whose sole purpose in life is to try and solve this problem. It would have no biases whatsoever, no biases toward selling, no biases toward not selling, it would try to take an objective view. Look at Customs who almost without exception since I've been here comes in at the last minute and picks up what pieces are picked up. I think that we ought to have enforcement go to Customs, based on just good old-fashioned track record, hard evidence. They come in and correct your mistakes and save Commerce, over and over again, as they did in this particular case with very little help and very little sharing of information throughout the process.

Well, I would agree with you that your MOU is an improvement. It doesn't go nearly as far as it ought to, but why the resistance to putting it in a statute? This resistance isn't any different from that of previous administrations either. Because administrations change, I feel that whatever is in this MOU, it ought to be in law. I hear that section 10(g) is all right; it's going to be handled by the MOU. Why not clarify it in law?

This administration is going to be here until 1988, but after that the Constitution says we will have a new one. Well, what is the attitude of that administration going to be? Are we going to go back to the attitude of the previous one who was lackadaisical to the whole thing? What are we going to get? I don't know. As I watch the Presidential primaries, we could have almost anybody President of this country the way the silly process works.

So I don't know what the future is going to hold. That's why I think it ought to go into statute rather than remain an MOU ac-

companied by bickering. So I sense, as I listened this morning, deja vu—there are different faces, different names, but the same testimony, same excuses, same results. The Soviets continue to profit by our technology and we continue to spend more on defense than we need to because of it and we can't get a handle on it. I don't know why. I've never been involved in one subject for so long during the decade that I've been in the Senate and experienced such great frustration and inability to get a handle on the problem.

Maybe I'll be sitting here during a future administration asking the same questions and hearing the same testimony from different people and different faces. They're all trying, they're all sincere, and again I don't question that. I believe that somehow we've got to minimize what is going on to aid and abet our enemies, and I'm probusiness. I have a reputation of being probusiness, but maybe our businesses are so anxious to do a pittance of sales or save a few jobs that they will sell anything to anybody as long as they can make a profit. Like I say, that's coming from Jake Garn, Mr. Conservative Republican, probusiness.

My probusiness attitude only extends so far and it stops at helping the Soviets to endanger this country and cause us to spend billions and billions of unnecessary dollars.

AUDITS OF DISTRIBUTION LICENSES

Mr. Archey, how many audits of distribution licenses were conducted between 1976 and 1984?

Mr. ARCHEY. Until 1984, I don't believe there were any. In 1984 we are doing an audit of the distribution licenses at the headquarters in several foreign countries.

The CHAIRMAN. I'm aware of at least one audit in 1977 that found 100 violations.

Mr. ARCHEY. That's correct. In 1976 there was an audit of a Geneva office with over 111 violations, and then when those violations were raised and surfaced in a report we asked for further information and the information wasn't provided and the license was suspended for 11 or 12 days.

The CHAIRMAN. For 11 or 12 days for 111 violations?

Mr. ARCHEY. Well, most of them were very minor technical violations regarding not merely terms of how the files were maintained and the information in them, but most of those were not of any—in fact, were of any significant violations. But the fact was that we asked for further information and it wasn't provided by the company and until the information was provided. to my knowledge, it's the only distribution license during that period that was suspended for failure to provide adequate information.

The CHAIRMAN. Do you have an overabundance of wet noodles to slap their hands with?

Mr. ARCHEY. Well, suspension of a distribution license is an extremely heavy sanction, particularly for companies of that size.

The CHAIRMAN. I would agree if it lasted very long, but 10 or 11 days, I don't see that that is a severe penalty.

Mr. ARCHEY. No, I would agree, but I think the point I would make—I haven't read the audit in all of its detail, but the information that we asked for and was analyzed by the audit was insuffi-

cient and if the information provided wasn't sufficient it would have been suspended for longer.

The CHAIRMAN. My next question would be that that audit was in 1977 and however superficial technical violations have been, there have been no audits until 1984. You don't follow up with people? This is the Senate Banking Committee. When there are problems with banks and they have an examination and find problems, the regulatory authorities go back and reexamine them. You go 7 years and don't bother to have another audit?

Mr. ARCHEY. No. I would agree with you. The point I would make to you, to go back to your earlier comments, I think this is a very different Commerce Department than the ones you have experienced in the last 10 years. In fact, in the entire period of the 1970's, not just distribution licenses but distribution licenses specifically, we saw a major erosion of the regulations governing the distribution license program. In 1969 it was called the warehouse inventory program.

The U.S. Government prior to the days of concern of extraterritoriality, approved the customer of the consignee overseas. Furthermore, we required monthly reporting against the license. There was a severe requirement in terms of description of the products, the sales territories were quite limited. In fact, the original distribution license program in 1968 was a program that was envisioned only to be for CoCom countries. It was expanded about 2½ years later to the entire world, for all practical purposes.

In 1978, Senator, the requirement for reporting against the license, which was basically an interagency agreement with the Census Bureau, in which we would get SED's and see what the shipments were against the license. That was stopped. The reason it was stopped was because it cost $250,000 a year. There was one person reviewing distribution licenses and so there was really no sense in spending $250,000 to review the shipments with one person being able to do it, as well as having to administer and process ongoing distribution licenses.

Last year, as a result of Secretary Baldrige's concern over distribution licenses, we began a 10-month review of them. We came up with the fact that there were lots of problems that occurred long before this administration that allowed that program to erode.

EXPANDED PERSONNEL FOR EXPORT ENFORCEMENT

We have an authorization to hire 25 people. We have 19 onboard. We have begun to do audits. We've done five or six audits so far in just the last few months. We're doing a major audit of the Digital Equipment Corp. I would also say to you in terms of the role of the Commerce Department and Trade Administration where I am, most of the increase in resources in Trade Administration, in the last 2 years, we've been the only aspect of ITA that has had increased budgets. Most of those increased budgets came from internal reprograming that came from the trade promotion, trade development, and international economic policy area.

Since Secretary Baldrige became Secretary in 1981, the export administration area licensing has gone from 131 people to 236 people and export enforcement has gone from 39 to we hope by

June to have 172, and although some of those were increased appropriations, a very substantial percentage of that came from other aspects of the Department.

So I do think that this Commerce Department is concerned about the distribution licenses and I share your concerns about the distribution licenses. I happen to be taking quite a bit of heat from business about proposed regulations because in fact we're dealing with that. We're dealing with it directly. And there's been an assertion made that the only reason Commerce came out with these license regulations is to deflect Steve Bryen and his colleagues in the Defense Department. That is not true. We started that program last March, but we came to the fall and came to realize there were a lot of problems. We also knew, given the import of the distribution licenses, we'd better do this right. We would have gone out with those regulations in December except the *MRI* case hit the papers and if we went out with the regulations it was felt it would be seen as an attempt to defuse that publicity, so we held it another month by my direction so we could go out and have it be seen independently and in its own right. We think those regulations are the right step. We think they are very strong. There may be some changes in it, but the basic objectives are there. Companies are going to have to say specifically what is the product. They are going to have to report. We are limiting the size of the sales territories. And last, we are trying to deal with an issue that is extremely difficult. We've had some discussions with Defense and others which is when that technology and products leave the country, it goes to an approved consignee. We think we do a pretty good job with the consignee. The issue is where does the consignee sell it. For non-CoCom countries, we are requiring that the consignees provide a list of their customers. That is creating enormous difficulties overseas because of so-called extraterritorial reach, but the U.S. Government has got to know where commodities go beyond the first tier receipt in any foreign country, and that's what we are trying to deal with.

The CHAIRMAN. My time is up on this round but I again would agree with you. There has been improvement and we can argue about whether there has been enough or not. I don't happen to think that there has been enough, but I would just ask you one more question on this round.

Why do you resist putting the MOU in statute so we don't go back to what you were describing before?

Mr. ARCHEY. I think the primary reason is that it's the view of the White House and the administration and I believe the President in terms of the fact that he does not want to have something etched into the legislation whereby how the administration or a subsequent administration may want to run the export control program is limited by statute. I happen to personally believe that in terms of both MOU's, both with Defense and particularly the one with Customs because of having been with both agencies, the issue is there is no reason to have any turf fights. There is no reason that that MOU and the Customs MOU can't be done as well and ultimately it will benefit the Government and the national security of this country. I think we are serious about it. We have had a lot of meetings about it. I think right now it just comes down to good

will because I do think both agencies operating in enforcement makes sense.

Mr. Chairman, to talk with the licensing function in terms of enforcing, the licensing function has to have an enforcement arm. The coordination problems are going to be monumental. It's taken us 18 months to bring the licensing and enforcement people together in such a way that they are no longer seeing things differently and they operate together daily and we finally established 2 months ago a joint group of engineers and enforcement people. We are already, as a result of this, analyzing historical data. We've got 35 major leads in investigation. That's just the beginning. But I think now, after having that corporate memory experience—and it hasn't been easy—I think the idea that there wouldn't be an enforcement arm of licensing would be a mistake for the national security.

The CHAIRMAN. Senator Proxmire.

Senator PROXMIRE. The chairman indicated that this administration would be in office until 1988. Now that's a wish and a possibility but it's hardly a probability. Well, let me put it this way. It may be a probability, but it's certainly not an inevitability.

At any rate, the main point or one of the main points the chairman was making is that we ought to put this into law because we will have other administrations and there's a good chance you'll have a Mondale, or Hart, or Jackson, or some other administration in 1985 and——

The CHAIRMAN. That isn't what I said. I said 1988.

Senator PROXMIRE. Well, I said it's a possibility. You didn't listen. You were talking to one of your experts and you missed the fact that I said your statement about 1988 was perhaps a probability but not an inevitability. But I certainly agree with your statement that we need statutory changes and not just MOU's.

Mr. Archey, I'm going to come back to you with questions in a couple minutes. First, I want to go to Dr. Bryen and Mr. Rudman. Before I do that, I want to say it's absolutely incredible that you had over 100 violations the last time you had an audit of a distribution license, and you haven't had any audits in this administration until 1984, until after the VAX computer diversion hit the headlines. Then you had an audit, not until then.

Now, Dr. Bryen, one reason we are focusing on the VAX computer diversion to the Soviets is because we believe, as you state on page 2 of your prepared testimony, that "this one case is only a symptom of the diversion problem"—sort of the tip of the iceberg. Can you give us your reasons for making that statement?

PROBLEM IS FAR GREATER ACCORDING TO REPORTS

Dr. BRYEN. Yes, I think so. This is one case that hit the headlines, but through the reports we constantly get in intelligence reports it appears to us the problem is far larger, not only in the cases involving American equipment but cases involving equipment to other Western countries. If you think there's enforcement problems here, I think I need to state on the record that there are even more severe enforcement problems elsewhere where in many cases even some of the CoCom countries lack the legal mechanisms to en-

force technology transfers problems. So there's a long way to go to get a coordinated system and we have emphasized as much as we can to our allies the importance of moving ahead smartly on this.

Senator PROXMIRE. You said at one point, as I understand it, this is the largest single diversion to date.

Dr. BRYEN. Attempted diversion.

Senator PROXMIRE. Mr. Rudman said the largest diversion in history. You cannot be sure of that. I think the chances are that we face the tip of the iceberg and therefore there are diversions far greater that we don't know anything about.

Dr. BRYEN. I prefaced my statement to say it's the largest attempted diversion because we got this one back.

Senator PROXMIRE. The largest diversion we know about?

Dr. BRYEN. That we brought back. I want to make that very clear. Let me furthermore say that it's only really under this administration anything has been brought back, that there's been many millions of dollars' worth of equipment that has been seized—more than that. I think also that we can take some credit, particularly in East-West relations processing or West-East, that we have a licensing mechanism that's working. It's far tighter than ever before.

What's happened, sir, is, I think, in part is that as the licensing West to East process has been tightened, made more sound, the Soviet efforts at diversion has grown commensurately because they're not going to get sensitive equipment through the licensing process.

Senator PROXMIRE. Now on page 4 of your prepared testimony you state that in order for Congress to cut our defense budget, it must first get serious about cutting off the flow of our militarily critical technology to the Soviets.

Do you agree with my contention that unless we cut off the illegal acquisition of our technology by the Soviets, our own defense research expenditures are in effect subsidizing the Soviet defense budget?

Dr. BRYEN. I agree, absolutely.

Senator PROXMIRE. On page 2 of your testimony you state that seven containers shipped from South Africa by Mr. Mueller's Soviet shell company were captured by the Customs Service working with our German and Swedish allies. You also state, however, that you "have now concluded that another eight containers full of sensitive commodities may have reached the Soviet Union."

Dr. BRYEN. That's correct.

Senator PROXMIRE. Can you tell us how and why you have reached that conclusion and indicate what might have been in those eight containers?

Dr. BRYEN. I think I can say generally that we understand that semiconductor manufacturing equipment that happened to have been licensed to MRI has not been recovered. We don't know where it is, but the proper assumption would be I think that it's in the Soviet Union.

Senator PROXMIRE. Do we know what was in those containers?

Dr. BRYEN. We have some indication of what possibly got through.

Senator PROXMIRE. Do we know that it would be of military value to the Soviet Union?

Dr. BRYEN. Absolutely.

Senator PROXMIRE. And of significant military value?

Dr. BRYEN. Absolutely.

Senator PROXMIRE. Dr. Bryen, on pages 4 and 5 of your testimony you refer to the recently concluded memorandum of understanding between the Commerce and Defense Departments that gives Defense a right to review individual validated licenses for 7 categories of sophisticated products to 12 non-Communist countries where diversion of our technology to the Soviets takes place.

Can Defense under that agreement with Commerce also examine high-technology goods shipped under distribution licenses to those same countries where diversions take place?

Dr. BRYEN. We have a slightly different arrangement on distribution licenses and we're going to begin working on those cooperatively with the Commerce Department. So the answer is, in general, yes.

Senator PROXMIRE. You say that you can't examine those?

Dr. BRYEN. Well, we've never worked on these types of licenses where they are validated West-West except on very limited ones and certainly not on distribution licenses at all in the past.

Now we will, under the President's decision which we support, begin to play a role in that process. But I want to caution you, Senator——

Senator PROXMIRE. Let me just interrupt at that point because what I'm getting at is under the memorandum of understanding between Commerce and Defense, Defense still has no right, as I understand it, to review distribution licenses, only individual validated licenses.

I understand that procedures for review by DOD of distribution licenses are still being negotiated and Commerce is resisting. Isn't that true?

Dr. BRYEN. I don't know of any resistance by the Commerce Department on this matter. The President has made a decision and we have to implement it. Up to this point, frankly, in the short time, what we've sought to do first is to organize our own capabilities in-house because we have *x* number of personnel to help us in the process and we want to use them with the maximum efficiency. So we will come to that, but there has not been any resistance by the Commerce Department whatsoever on that.

Senator PROXMIRE. Mr. Archey.

Mr. ARCHEY. Could I answer that because I think it's important to expand on that, what the President's decision was. The President reaffirmed what had been since last June a negotiating potential MOU with Defense on the individual validated licenses as stated. The second aspect of the President's decision is that he agrees and he affirms in principle Defense having the right to review distribution licenses. That will be in a staggered manner. As Steve has suggested, we're going to have to do a fair amount of coordination and getting our respective acts together to make the individual license program work smoothly and there will be established, Senator, a review group under NSC leadership and direction that will basically monitor the implementation for 3 or 4 months

the individual licenses. Then, if all goes well in that, there will then be the beginning on a pilot basis distribution licenses will begin there and assuming that things go well, it would be expanded as is appropriate.

So the principle of the right of Defense to review distribution licenses has been affirmed by the President.

Senator PROXMIRE. Well, it sounds to me like it may not be the kind of firm explicit understanding we want. It certainly is not the statutory provision which I and the chairman agree is needed.

Dr. Bryen, reminding you that you are under oath, I ask your personal view on whether you favor the reforms in the Senate bill that give the Defense Department a clear statutory right to review militarily critical exports to non-Communist countries where there are clear risks of diversion of such technology to the Soviet bloc.

SHOULD CUSTOMS ENFORCE OUR EXPORT LAWS?

Could you also give your personal view on whether you believe Customs rather than Commerce should enforce our export control laws as provided for in our Senate bill?

Dr. BRYEN. Well, my personal view, Mr. Chairman, is that we should give as much help to the Customs Service to carry out its responsibilities as we can. As you know, one way we have done that already is that the Defense Department has made available to Customs some $28 million in support initially to get——

Senator PROXMIRE. I want you to respond to the particular question I asked, not whether we're giving them as much help as we can, but whether we should give them a clear statutory right, whether we should write it into the law. I want your personal response.

Dr. BRYEN. I think they're doing that now, sir.

Senator PROXMIRE. All right. Go ahead.

Dr. BRYEN. I believe that it's a better question to put to the Customs Service whether they think they have sufficient authority. What I've found so far is that it's been a very valuable asset and we have been pleased to be able to support it and we will continue to do that and we can support it. That is to support it not only in terms of financial support, as we had to do on one occasion, but also to provide to Customs some of our expert technicians to help them pinpoint those sensitive exports and where to look.

Senator PROXMIRE. I want your personal view. You're representing the Defense Department. I want your personal view as to whether the Defense Department should have a clear statutory right to review militarily critical exports.

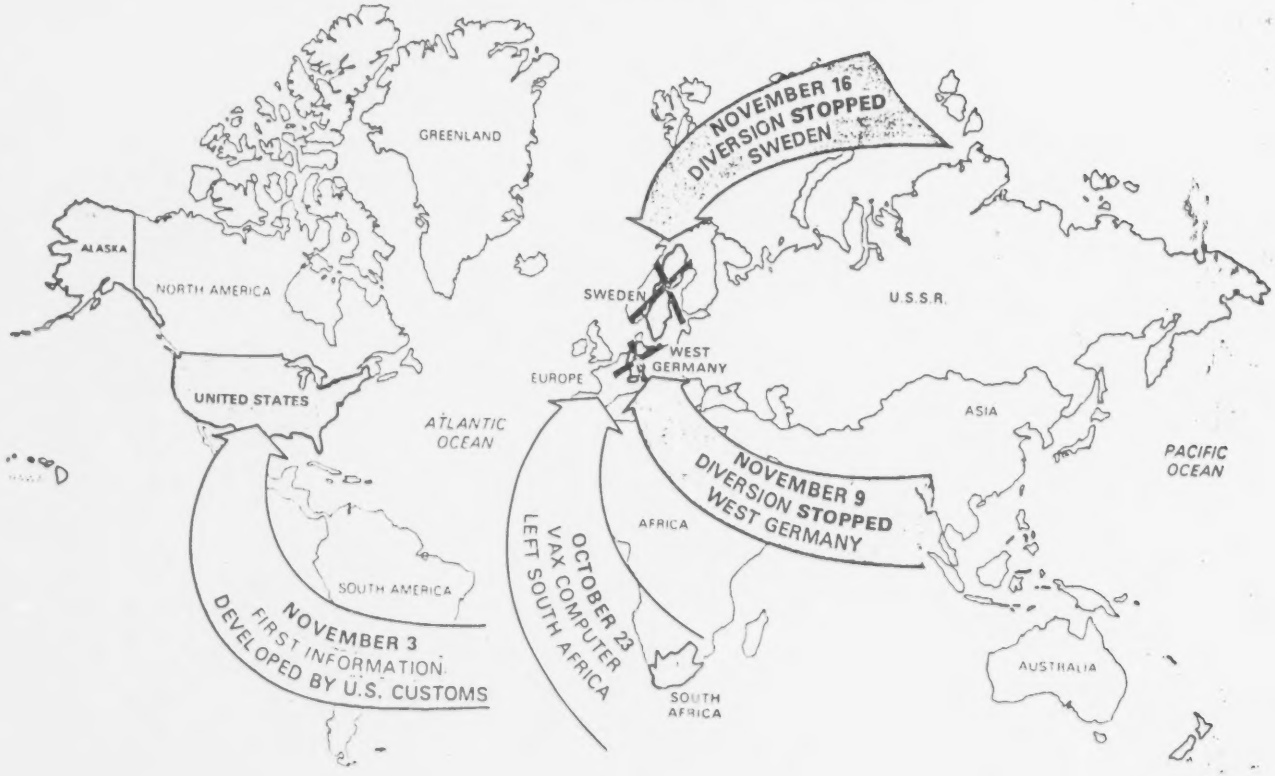
Dr. BRYEN. Well, we think it should have and we think it does.

Senator PROXMIRE. All right. My time is up. I have other questions.

The CHAIRMAN. Mr. Rudman, the committee requested that you bring along some charts depicting major events in this case and I would appreciate it if you would present those charts and describe them to the committee at this time.

[The following charts were submitted for the record:]

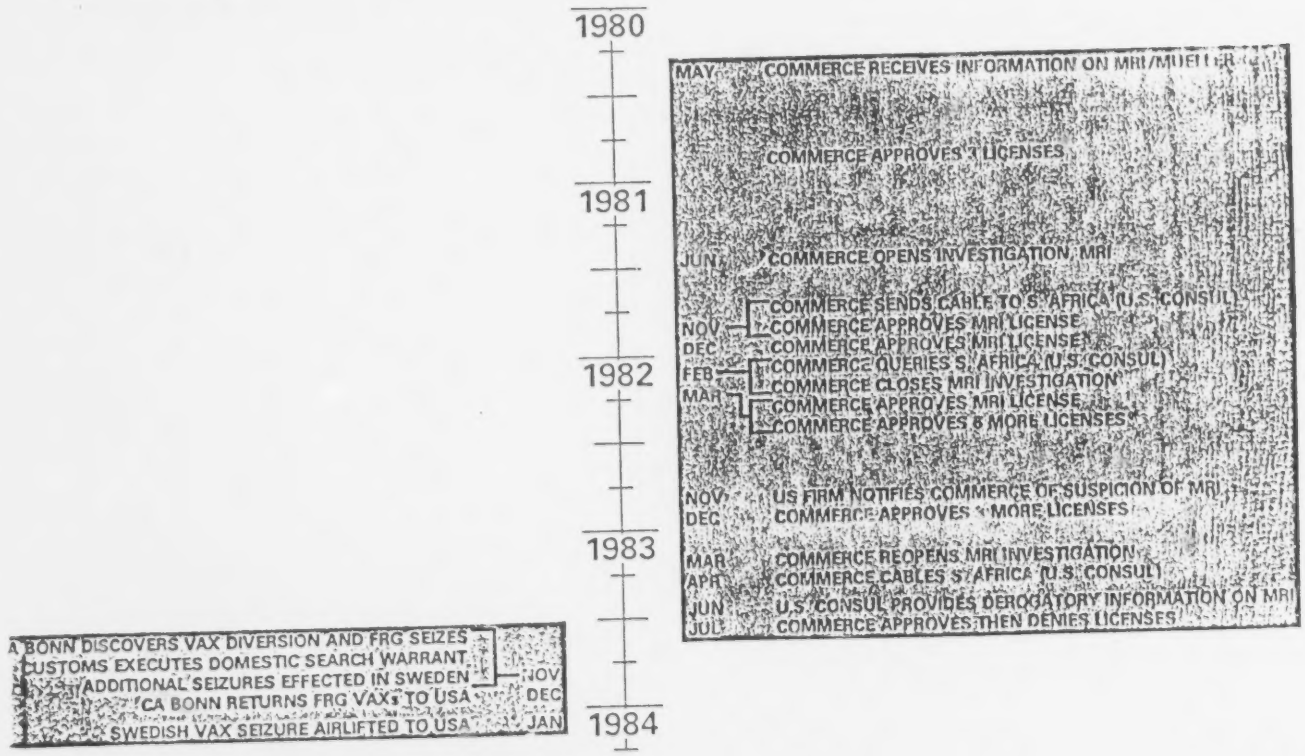
VAX COMPUTER DIVERSION TO U.S.S.R. via SOUTH AFRICA



MRI/MUELLER: VAX CASE

U.S. CUSTOMS SERVICE

DEPARTMENT OF COMMERCE


1980
1981
1982
1983
1984
MAY COMMERCE RECEIVES INFORMATION ON MRI/MUELLER
COMMERCE APPROVES 1 LICENSES
JUN COMMERCE OPENS INVESTIGATION, MRI
NOV COMMERCE SENDS CABLE TO S. AFRICA (U.S. CONSUL)
COMMERCE APPROVES MRI LICENSE
DEC COMMERCE APPROVES MRI LICENSE
FEB COMMERCE QUERIES S. AFRICA (U.S. CONSUL)
COMMERCE CLOSES MRI INVESTIGATION
MAR COMMERCE APPROVES MRI LICENSE
COMMERCE APPROVES 6 MORE LICENSES
NOV US FIRM NOTIFIES COMMERCE OF SUSPICION OF MRI
DEC COMMERCE APPROVES 3 MORE LICENSES
MAR COMMERCE REOPENS MRI INVESTIGATION
APR COMMERCE CABLES S. AFRICA (U.S. CONSUL)
JUN U.S. CONSUL PROVIDES DEROGATORY INFORMATION ON MRI
JUL COMMERCE APPROVES, THEN DENIES LICENSES
A BONN DISCOVERS VAX DIVERSION AND FRG SEIZES
CUSTOMS EXECUTES DOMESTIC SEARCH WARRANT
ADDITIONAL SEIZURES EFFECTED IN SWEDEN
NOV
D
CA BONN RETURNS FRG VAX TO USA
DEC
SWEDISH VAX SEIZURE AIRLIFTED TO USA
JAN

Mr. RUDMAN. Certainly.

The CHAIRMAN. Mr. Archey, while we're setting those up maybe I could just ask you one question. What was your recommendation to the Office of Export Enforcement on the VAX 11/782 license request to the Mueller firm, MRI?

Mr. ARCHEY. At the point it came in? There was no negative information and in fact it's my understanding that it was just a cursory review and there was no recommendation for or against.

The CHAIRMAN. It was not a recommendation of approval?

Mr. ARCHEY. I'm not sure if my record shows—it's my understanding that the *MRI* case when it first came in in September 1982 through the normal review process and would have been a recommendation for approval. It was then turned back and came back in and was not reviewed a second time by the Office of Export Enforcement.

The CHAIRMAN. I will turn back to Mr. Rudman.

Mr. RUDMAN. Yes, sir. The chart in question which reviews the activities of the two agencies involved in the investigation since the inception in 1980 needs some explanation. We first in Customs became aware that the Commerce Department had previous information back as far as May 16, 1980, that the Richard Mueller firm Semitronic was attempting to procure an ion implantation system from MRI. We learned this on December 1, 1983, as a result of a chance meeting between a Customs special agent under my supervision and the Commerce OEE special agent who had pursued that lead back then for Commerce.

ORIGINAL INFORMATION RECEIVED IN MAY 1980

Commerce received the original information back in May 1980. This information linked Richard Mueller, who was already a fugitive in a joint Customs-Commerce case, and Mueller was known to this particular Commerce agent. It linked Mueller, his firm in Europe, Semitronic, and MRI. The Commerce agent told the Customs agent he was familiar with the previous investigation. He had participated in the investigation in which Mueller was indicted in California and he immediately recognized Semitronic was in fact a Richard Mueller controlled firm.

As you can see, between the time that Commerce received the information on MRI and Mueller and Semitronic in May 16, 1980, and the time they opened the investigation on June 16, 1981, they issued three validated export licenses in the value of $745,000 in favor of MRI, the first being May 19, 1983, 3 days after they were provided the derogatory information involving this ion implantation system.

No investigation was conducted. Rather, the Commerce agent cabled the U.S. consulate in Capetown and requested that they discreetly interview one of the principals at MRI to determine the veracity of the allegation.

The officer who was identified for interview by the Commerce agent to the consulate was the same MRI employee who had signed the document certifying U.S. commodity replacements would not be diverted or otherwise improperly used. He was interviewed on several occasions by a foreign commercial service officer who was

neither trained nor experienced in conducting criminal investigations.

On the basis of the denial of any wrongdoing by the MRI officer, Commerce terminated its inquiry with no further action.

Prior to November 22, 1982, many more licenses had been issued. On November 22, 1982, a Santa Clara firm, a public spirited firm, advised the Director of the Office of Export Enforcement that they were suspicious of MRI because they had purchased some equipment and did not request installation or inspection by the firm's personnel as specified in the sales contract, with the installation and inspection included in the purchase price. They also failed to order warranty replacement parts, a practice which is normal in every other installation of that company's similar equipment.

Four months after that, after the tip from the California firm, and after Commerce had licensed this VAX ultimately to be seized in Hamburg and after it had been shipped from the United States, then on March 24, 1983, Commerce requested the U.S. consulate in Capetown to conduct an onsite postshipment check with MRI based on the information they received from the California firm.

In this 4-month period, Commerce licensed two additional VAX 11/782 shipments to MRI during that same 4-month period.

On December 2, 1982, Commerce licensed to ship integrated circuits valued at $4,200 and on December 7, 1982, they licensed an ion implanting system valued at $401,000. In addition, they took no action on the shipment of this same company for their automatic inspection stations. Commerce was notified in the original letter to the California firm on that on November 22. In fact, those were seized by the Swedes in November 1983 and returned to the United States along with the other equipment.

On June 27, 1983, the consulate in Capetown responded to Commerce's March 24, 1983 cable by advising Commerce that the individual who had been the one interviewed all the time admitted that MRI was engaged in conduct inconsistent with the terms of the licenses granted to it.

The consulate recommended the MRI and this individual be denied permission to import any controlled items.

On July 5, 1984, Commerce approved a license for another VAX 11/782 to MRI but rescinded the license later that month. As far as I know, Commerce took no further action until after being informed by Customs of our investigation in November 1983. I believe the Customs aspect, is as I mentioned in my testimony, but I'll go on if you wish.

The CHAIRMAN. Please continue if you have any more detail you wish to give us on your charts.

Mr. RUDMAN. Behind there is simply representation of how Customs operated after November 3. We developed the information on the left-hand arrow on November 3. Following the October 23 sailing of the *Elgarn* from South Africa on November 9, as you can see, the diversion was stopped by the West Germans and on November 16 the diversion was stopped by the Swedes.

I don't think further explanation of the events prior to November 3 would be of any use. I can continue on with our cooperation with Commerce after that time if you wish.

The CHAIRMAN. Well, I would be interested in your description as well as Mr. Archey's if he desires, of what happened between July and November. What was going on between Commerce and Customs in the way of interagency cooperation, if any, during that period of time?

Mr. RUDMAN. Mr. Chairman, I can't respond to that because I don't have any idea what, if anything, they did during that period of time.

The CHAIRMAN. Mr. Archey, let me ask you, who did Commerce ask to investigate MRI in South Africa?

Mr. ARCHEY. You mean in May 1980?

The CHAIRMAN. Whenever.

COMMERCE SUPPLIED THE INFORMATION TO ALL PARTIES

Mr. ARCHEY. Well, I'd like to respond because all of the information Mr. Rudman presented is based on information we provided them which we have done not only completely but we did promptly.

No. 2 is I would like to again make the point, because I think this is one instance where it is an unfair rap, and that is that the May 16 sensitive information went to the Treasury Department, as Mr. Von Raap said in the closed hearing, it did not go on to Customs. Customs at the same time as the U.S. Commerce Department at that point had the same responsibilities under this act and so as I acknowledged in my opening remarks, the way the information was received and translated internally, until later in the year when the agent took the case on, he was receiving a translation, if you will, of very sensitive information that led the agent working the case to believe that MRI was the source of the information. Therefore, the good guy.

He then proceeded on that case based on that and not as presented in the normal way. He didn't open a case. What he did do was he did a postshipment check. But the point I'm making is that the Defense Intelligence Agency and the Treasury Department received this information all in the same day. And the other point I would make is in terms of some of the information about when we did it. In fact, in 1983 long before the second VAX case—the second VAX case, although the application came in, we questioned it. The second VAX application was not the VAX. It was for $200,000 software to go with the VAX. And the other one was the GSA—I'm sorry, we're not supposed to mention—some other semiconductor equipment. Both of those were denied internally prior to the diversion and Customs intervention on the basis we had internally, and so one was rescinded and one was denied outright.

The CHAIRMAN. But let me slow down because I just am not capable of understanding. You ask an economic officer in the Embassy, an employee of the State Department in South Africa, to investigate. Now is this done in normal communications in the pouches that go out, and isn't this only a small part of the economic officer's duties? Good heavens, when you find out about this man how can you sit there and make excuses all day long that everybody got the information at the same time? Doesn't anybody stay after work? Does anybody pick up a phone or do you just put it in a

pouch and that takes care of your duties for the day and—again, I'm not talking about you personally, Mr. Archey—I'm talking about a situation. Is there anybody in our Government that says, "Hell, this is important," and maybe make a call himself? Doesn't somebody get so excited that they get somebody on it besides an economic staff officer in the South African Embassy? Do you go from July until November with nobody talking? We do have a modern telephone system, and even though AT&T has been broken up, it still works, despite the cost. Does anybody say, "I'm worried about this because of the national interest." You know, as crazy as the Congress of the United States is, Senator Proxmire and I follow up on a lot of things personally. We don't wait for it to go through the pouches around here. We see each other and we make a call and we do something. Does anybody ever call and say, "Hey, we're really worried about this. There's a computer and this Mueller has a bad record that's been proven over and over again." Are we working together? Are we coordinating our efforts or are we not?

It sounds to me like this is just another bureaucratic bunch of baloney. How can you can sit here and excuse it all day long and say you took the proper steps? I am sure you probably did as far as fulfilling the requirements of the law go. You checked off the boxes and you put it in a diplomatic pouch and everybody got the information, but was anybody really concerned or do you just work from 9 to 5 and when the day is over you go home and you get your pay and your 30 days leave a year and all that? Is that what we're dealing with? Or does somebody care enough to do something on the weekend to follow up?

Maybe I'm overly simplistic, but that's what I would do if I was down there. I would call a Secretary and say, "Hey, we've got something that really smells here," rather than waiting from July until November or whenever it was. I don't see any reason to excuse what happened, no matter how much all of you can justify following the bureaucratic rules and regulations. I don't see why this happened and I don't see why it happens over, and over, and over again and why we can't get a handle on it.

Once again, I'm sorry to get so irritated about it, but after 9 years it gets a little bit frustrating when you just hear the bureaucratic excuses again and again. It will happen again, and you know damned well it will and I know it will until somebody really gets serious about it. It's going to happen again. I don't know whether it will be next month or next year, but something is being diverted out of this country right now because somebody isn't taking enough time to do something about it other than following the rule books like in the military, checking off the boxes, so they are clean.

You sit there and tell me that everybody got the information the same day—so what? What you're telling me is that everybody failed and then Customs finally picked it up in November or December. That is not a reason. Let's try and solve the problem.

Mr. ARCHEY. Senator, I think my response is that I'm not saying that because everybody got it that it's an excuse.

No. 2 is I think I said rather forthrightly both in my prepared statement and in response to several questions from both you and Senator Proxmire that we made mistakes. We in fact didn't do it right by the book or the checklist. We made mistakes. They were

compounded because when we got into 1981 the case agent, the person who originally received the information, was not in the Commerce Department. He did see the importance of it. He was somebody who had been around a long time and he was one of the very few veteran people. But in fact the person who was eventually assigned the case saw the information rightly as the case agent that the nature of the information as he saw it was that MRI was the source of the information saying that there may be this company trying to get stuff for us and they were seen as the good guy.

I'm also saying to you that we did during this period of time four prelicense checks and two postshipment checks with some people in the contents office who had some understanding of these issues and in fact were highly laudatory of the company and the principals. Also in terms of other companies who had been there who indicated this is a legitimate ongoing enterprise. You also have the organization that was associated with the University of Stahlenbaush, a very, very prestigious university in South Africa, two of whom, professors or members of the faculty, were on the board of MRI.

MISTAKE OF NOT CORRECTLY INTERPRETING ORIGINAL INFORMATION

There were a lot of other circumstances, but the point I would make to you and where I'm saying it is you can't justify it in the long run—if the original information had been correctly interpreted and communicated, then the rest of those would not have occurred, because in fact there would have been knowledge of what the connection between Semitronic and MRI actually was, and I am saying that is a mistake that was made and it's a terrible one. I am saying, though, that in terms of how we proceed from there, I think we did act responsibly and in fact when it came into 1983, this issue of what we were sharing—we weren't sure at the point in time that we were going to have a criminal case. We weren't sure whether there was going to be diversion. In fact, as you may know or as you do know, Senator, the concern we had initially verified by Mr. Harrison, the director, which is not found out to be true subsequently, our major concern in June 1983 was the possibility that this was internal diversion to South Africa governmental military use. It turned out that was not the case. Therefore, we had a question as to whether we went to South Africa and asked the South African Government to intervene because we would have been in a difficult situation that way.

I am saying the fundamental problem was made in 1980. In the same letter, that company said this in fact is unusual circumstances but they have probably the best engineer we know of to put it in place and that's probably what they did.

So what I'm getting to is I concede there were mistakes made. I think in terms of the information sharing with Customs, that's what the MOU is going to require, the exchange of cases being investigated overseas, so that we don't step on each other and we don't have unnecessary redundancy.

But the last point I would make, Senator, on that—and we only recently got this in March. We have had an outstanding request to the Customs Service since March 17, 1983, to give us a list of all

the names they have under investigation so we don't license one of those. We never received that information.

The CHAIRMAN. Mr. Rudman, you're shaking your head on that. What is your response?

Mr. RUDMAN. The other day I personally delivered an 800-page computer printout of all 13,500 names of persons involved in our export enforcement cases.

The CHAIRMAN. Why did it take 1 year?

Mr. RUDMAN. You're talking about the 1983 request?

Mr. ARCHEY. I'm saying March 17 the letter went to George Corcoran from Ted Wu saying we would like to exchange a list of cases under investigation. Our primary concern is that we not inadvertently license any cases that Customs may have under criminal investigation. We've received no response to that letter, despite two followup meetings in June until the MOU requirement on March 1 when we got the first 200 names.

No. 2, Bill, you and I know that those 13,000 names to us aren't going to be very helpful because it's just about every single suspect thing in the TEC system. It's unrefined and it's suspect. It's a lot of information that for all practical purposes Customs would have difficulty in being able to analyze. It's unrefined. It's not going to be that helpful.

What we are looking for—and I'm sensitive to it—Customs is a very decentralized organization, but all the cases being worked by the field offices we're not getting any because they're not being captured at headquarters. That's a large universe, much larger than the 310 cases we've received in the last 2 or 3 weeks.

The CHAIRMAN. Did it ever occur to you, to get back to my point about following through, that after you submit a letter and have some meetings at whatever level, to go to the Secretary of Commerce and say, "Mr. Secretary, we have a problem. Do you want to call Customs or do you want to raise hell down at the Cabinet meeting?"

It sounds to me like this is all occurring at some level where everybody is afraid to call or jump on anybody and as long as you have said you had another meeting and you didn't get an answer, that's your excuse. How does 1 year pass? What happened from July until November? What was Commerce doing from July to November? You approved one and then you turned one down. What did you do from July to November or December?

Mr. ARCHEY. We started action for denial order on MRI. In August 12 when we had enough reason to believe it was not an internal diversion to South Africa, we requested the South African Government's involvement to help assist us in the case. We put a stop on all further applications that were coming in, no further applications came in on MRI, but we put a stop on it.

The CHAIRMAN. I'm specifically referring to the VAX that had already been approved and I'm talking about the recapture that Customs did on the dock in Hamburg.

Mr. ARCHEY. No, we did not and we did not go into the company to see or to inventory what was there.

The CHAIRMAN. So you had nothing to do with it. You were going through the normal process of denying additional licenses but as

far as you know Commerce's enforcement division wasn't trying to figure out where the VAX was going.

Mr. ARCHEY. No, and I think that's a rightful criticism. When we went through this entire debriefing back in November or December with our entire enforcement office, that was the question I raised. I said when it got to be late summer, why didn't we go over to South Africa and say, "Where is this stuff?"

Part of the reason was because of the sensitivity regarding the potential for internal diversion and so we had to hold because we had to find out whether that was in fact maybe the case. And then when we got to the point of knowing that wasn't, we did aggressively pursue it.

I would also say, Senator, which hasn't been said today and I think it needs to be, this was big surprise I think to Steve's organization and to a lot of organizations because the last place in the world anybody thought diversion was going to take place was out of South Africa, and I think now we're all a lot wiser as a result of this.

The CHAIRMAN. Well, you're wiser, but you still oppose the provision in the bill to turn the enforcement capabilities over to Customs who over a period of years before this administration and throughout this administration has been about the only ball game in town on the enforcement end. The enforcement division of Commerce did nothing on this. If it hadn't been for Customs, that VAX 11/782 would be in the Soviet Union; right?

Mr. ARCHEY. I think if it weren't for the tip provided Customs, that is correct.

PRESIDENT'S DECISION IS HELPFUL TO DOD

Dr. BRYEN. If I could just intrude one second on this conversation, it seems to me that the President's decision helps us a great deal. There's been a lot of discussion about who did what to whom. The fact is that even though there's intelligence information in the system, it does not necessarily tie that intelligence to a license or provide others with knowledge that there's a license in process.

If you look at the *MRI* case, a fundamental question should have been asked—not about whether there's internal diversion to South Africa—the fundamental questions about what are they doing with this technology in South Africa and where is it leading to? It has a very heavy military value because it's a low-power, very specialized kind of technology used in military systems. You ask, "what's going on?" We think that's the kind of question the Defense Department would have raised. We would have gotten even further along the way. We would have raised the question in other cases, just as we did in another West-West transfer which we worked cooperatively on an interagency basis and found a good solution.

So you're absolutely right in stressing the importance of the agencies working together. It's absolutely vital that we share data base. It's got to be 100 percent. It can't be 70 or 40 percent. The cooperation just has to be there. And bring to bear skilled people that exist in the Government. There are skilled people in the Government to deal with this. There will never be 100 percent guaranteed perfection, but it will go a long way and that's why I think the

President's decision is right, why the monitoring by the National Security Council is terribly important because they are not weighed down by a turf battle of any type.

Just a last point I think I should make in that connection. We do have a responsibility to be efficient. There is a problem of delaying trade. I think everybody understands it. We are committed in the Defense Department to be as rapid as we can to automate as much as we can so that we will not delay legitimate trade. We would not want such delays to happen.

The CHAIRMAN. Gentlemen, my time is up on this round. I've used all of mine and all of Senator Proxmire's time. So he gets double time on this next round for being so patient and not kicking me in the shins for going on and on. If you would excuse me just a minute while Senator Proxmire questions, my Governor is waiting outside and I will be back shortly. Senator Proxmire.

Senator PROXMIRE. Mr. Rudman, on pages 2 and 3 of your prepared testimony, you refer to meetings on November 8, 1983, between Customs, Commerce, and Justice in which you were trying to develop information that the goods on the ship being detained in Germany were intended for the Soviets. The Germans, we understand, needed this information to have probable cause to seize the shipments.

Do you believe that Commerce officials cooperated fully with Customs and Justice officials at that time? If not, what did they not do that they could have done?

FULL COOPERATION OF COMMERCE WAS LACKING

Mr. RUDMAN. No, sir, they most certainly did not.

Senator PROXMIRE. They did not cooperate?

Mr. RUDMAN. May I explain?

Senator PROXMIRE. I wish you would.

Mr. RUDMAN. The Department of Commerce was first informed of Customs investigation of Richard Mueller at approximately 2:30 p.m. on November 8, 1983, during an emergency meeting on the subject involving the Internal Security Section of the Department of Justice, Customs, and Commerce. This meeting was requested by Customs and we specifically requested that special agents of the Office of Export Enforcement be there.

As you say, this was when we were both trying to get the problem of our search warrant in New York and give the Germans enough to take the action that they were required to take. At the mention of the identity of the South African intermediary in the case of MRI, one of the OEE officials noted, "We have an interest in MRI" and "You have probably seen our cables on MRI." And nothing more.

At the meeting, Customs offered all that it knew of the instant allegations and stated that it welcomed further information regarding the alleged violators and/or violations from anyone. There was only silence.

The seizure which was made by the German Customs Service on November 9 was based on the thinnest evidence of potential diversion and because of this the first German court refused the applica-

tion for the search warrant, and one of their circuit courts finally approved it but very nearly refused it.

None of the information which Commerce had on the Mueller/MRI/Soviet connection was made available to Customs for use in spite of our request on November 8.

On Monday, November 14, we learned from our special agent-in-charge of New York that their review of documents which had been obtained during a search warrant of a New York firm that in this search they found a business card of an OEE investigator on the premises. Both the records reviewed and the coincident interviews of the firm's employees revealed that one of them had been in frequent contact with OEE. Our agents were concerned that they had made a visit to the New York firm and they so informed our headquarters. Immediately upon receipt of this information, we initiated telephone calls to Commerce to determine if they had ever visited the New York firm, if Commerce had had any contact with anyone in that firm of potential relevance to a now established criminal investigation and, most importantly, if Commerce had any information of any kind regarding the possible culpability of any U.S. or foreign persons in this entire matter.

Commerce advised us at that time that they had visited the New York firm but their contacts were innocuous, and they had nothing which may help us in the way of establishing the culpability of involved parties.

On November 15, I personally telephoned Commerce Deputy Assistant Secretary Theodore Wu and asked him if he was familiar with the *Mueller* case which had been featured in the press on that same day. Mr. Wu said that he was and that Commerce had some information about MRI but as a condition precedent to sharing such information Commerce would insist that the investigation be conducted jointly and that Commerce be allowed to send investigators to South Africa with the Customs investigators. We told Mr. Wu that we would cooperate but the Customs had an ad hoc arrangement with the South Africans and adding Commerce investigators and broadening the inquiry to other dealings other than the instant shipment was a South African Government and not a U.S. Customs decision to make.

Also, on November 15, customs special agents went to OEE and provided them with as complete a briefing as possible on the current status of the *Mueller* case and answered all the questions that we could answer at the time. We requested that we be allowed at that time to review any DOC/OEE file on MRI or Mueller, but none was made available. Further licensing information was promised.

On November 16, 1983, Customs special agents and OEE agents Cuthbert and O'Neill met to discuss the possibility of OEE participation in the South African investigation of MRI. When specifically asked if OEE had anything to offer with regard to the transactions under investigation between the New York firm and MRI, OEE responded that they did not. This occurred on at least three occasions during the conversation and at one point Mr. Cuthbert also denied that OEE had anything on the principal suspect, Richard Mueller.

On the morning of November 17, 1983, and during the preparations for travel to South Africa by Customs special agents, OEE agent Cuthbert was again requested to provide any information of any kind in the possession of OEE regarding the possible culpability of U.S. or foreign persons or interests in the *Mueller/MRI* case.

During the morning of November 18, 1983, and the course of a briefing by Customs to the National Security Council [NSC] and all agencies interested in the Mueller/MRI shipments, OEE agent Robert Rice noted that some $8 million of U.S. technology had been licensed by Commerce for shipment to MRI. Mr. Rice also stated that MRI had been under investigation for some time. Both the DOJ representative and the Customs briefer concluded immediately after the briefing that there was a strong possibility that information of an evidentiary nature existed in OEE files. During the briefing, representatives of the Department of Defense [DOD] commented that it had never reviewed the MRI license applications and that the sale and shipment of VAX 11/782 computers would not have been approved to South Africa if DOD had been given the opportunity to review them.

After the NSC briefing, Customs attempted to contact Mr. Wu concerning the OEE statements. Assistant Commissioner of Customs for Enforcement George Corcoran telephoned Mr. Wu and stated that he understood from OEE comments at the NSC briefing that Commerce had documents concerning MRI and that Customs needed them. Mr. Wu said there were license applications and some background data. Mr. Wu told Mr. Corcoran that these documents would be provided, but that time was needed for copying.

Later on November 18, 1983, Customs agents went to the office of Commerce Deputy Assistant Secretary Theodore Wu. The Customs officers had been advised by Customs Assistant Commissioner Corcoran that he and Mr. Wu had agreed that OEE would turn over all of their files on MRI/Mueller to Customs for use in the Customs investigation. Throughout the meeting, Mr. Wu was visibly agitated and stated that "you could have settled this long ago" and that "if you would have let our guys go to South Africa we wouldn't have this problem." Mr. Wu referred, on several occasions, to the meeting on November 16, 1983, between Commerce—OEE—and Customs and said "I thought we had a deal then." Customs summarized the November 16 meeting, noting that it was a decision of the Treasury Department—not Customs—that, if OEE had nothing to offer regarding the New York to MRI shipments, there was no need for OEE to participate in the South African part of the investigation. At this, Mr. Wu noted that OEE had nothing on MRI/Mueller, but he added that OEE did have a criminal case against MRI. Mr. Wu never identified any possible U.S. coconspirators with MRI in this criminal case.

Mr. Wu said that his agreement with Mr. Corcoran involved only licensing information and not investigative files. Customs then asked for any information in any file which would indicate the culpability of anyone in this case. At this, Mr. Wu noted that the matter of a release of investigative files would have to be referred to Mr. Lionel Olmer, Under Secretary of Commerce for International Trade. As to the question of any files on the New York firm, one of Mr. Wu's staff responded, "we don't have an investigative

file jacket on the New York firm." The only documents released to Customs on the evening of November 18, 1983, consisted of licensing information and license application copies.

Senator PROXMIRE. So the gist of this is that Commerce had this information. They knew that you had to have it in order to have probable cause and you didn't get the information? Isn't that right?

Mr. RUDMAN. Yes, sir, all that information, as Mr. Archey correctly stated, came from Commerce, but it didn't come until after the relevant dates and after our agents had left for South Africa.

Senator PROXMIRE. Before I ask Mr. Archey to comment, can you tell me if you have any reason or did they give you any reason as to why they wouldn't provide the information? What would you suspect was the reason?

Mr. RUDMAN. Well, the only reason given—I wouldn't want to speculate on why otherwise—but the only reason given was Mr. Wu's statement to me that they wanted to participate in the investigation and we wouldn't get anything until we let them do it.

Senator PROXMIRE. Mr. Archey.

Mr. ARCHEY. Well, first of all, I want to congratulate Mr. Rudman on his spontaneous off-the-cuff response to your question and, No. 2, is——

Senator PROXMIRE. You're not quarreling about his right to prepare very carefully a response?

Mr. ARCHEY. Not at all. It's thorough.

Senator PROXMIRE. After all, we can't always trust our memories on such matters. Even Commerce can't do that.

Mr. ARCHEY. We make mistakes on occasions.

The second point I would make is that I got into this after the dates Bill was talking about and it's around November 16 or 17 in which Ted Wu came to me and talked about it and I made it clear to him and I talked to the Deputy Assistant Secretary for Enforcement for Treasury and I said I'm not going to hold anything back. There was a meeting held either that Saturday afternoon or that Sunday at my direction, and my directions to my people were very explicit—give them what they need, period, and don't hold it back. If there were problems prior to that, I wasn't aware of them. When I became aware of them, I took action immediately to change that.

Senator PROXMIRE. All right. Mr. Rudman, can you describe for us the results of the investigation carried on by Customs into Mr. Mueller's activities in South Africa and elsewhere since November 3, 1983?

Mr. RUDMAN. Yes, Senator, due to the strategic importance——

Senator PROXMIRE. Is this going to be a long response?

Mr. RUDMAN. Yes, sir.

Senator PROXMIRE. Can you summarize it for me?

VAX CASE RESULTS IN INTERNATIONAL COOPERATION

Mr. RUDMAN. Since this investigation was initiated, the Customs Service has been able to link numerous other known diverters to Mueller and his Swedish business partner. As an example, it has recently been discovered that Customs fugitive Brian Moller-Butcher has utilized Mueller's Swedish partner to divert strategic commodities to the East bloc. As a result of an intense investigation

conducted by the Swedish Government, a shipment of U.S.-origin semiconductor manufacturing equipment was seized on January 24, 1984, as it was transiting Sweden en route to East Germany. This illegal diversion has been linked to Moller-Butcher.

Due to the strategic importance of the VAX 11/782 computer system, Customs initiated a trace on all such systems. The manufacturer provided a list which identified all sales of VAX 11/782's. In all, approximately 153 VAX 11/782's have been marketed including the system which was recovered in the Hamburg container. The Customs Service has recently developed reliable information that one of these VAX 11/782 systems was successfully diverted to the Soviet Union. It has been learned that the system was exported to Western Europe and subsequently diverted to the Soviet Union through the Mueller organization. As this matter is still under investigation, no further details may be disclosed at this time.

During February and March 1984, a multiagency review panel evaluated the computer equipment returned to the United States by Swedish and West German authorities, as well as the semiconductor production equipment licensed by Commerce to MRI—that equipment was successfully diverted from South Africa prior to the Swedish and German seizures and Customs investigation. The conclusions reached by that panel, indicated that the Mueller organization had successfully diverted millions of dollars of U.S. high-technology equipment. These diversions have had an adverse impact on the national security of the United States—the details of this analysis are classified.

After the equipment was inventoried by Customs personnel, a series of undeveloped leads were prepared for dissemination to Customs field offices around the world. Preliminary investigations by these field offices indicate that much of the U.S.-produced equipment acquired by the Mueller organization was purchased in Europe where it had arrived by means of Commerce's distribution license system. This includes equipment manufactured by at least three other prominent U.S.-based firms. These leads will be expanded in order to develop further information regarding the criminal culpability of these firms. Documentation already reviewed reflects that they sold licensable equipment to Mueller through his German and Swiss subsidiaries long after Mueller had been placed on DOC's economic defense or denial list.

Since the initiation of its investigation, the Customs Service has worked closely with West German authorities. The West German State Prosecutor and the Customs investigations office in Lubeck have been conducting a far reaching probe into all of the activities of Mueller and his associates, including Customs fugitive Volker Nast, former DEC employees Manfred Schroeder and Norbert Stoltenberg, Mueller's brother-in-law Harold Bickenbach and five other West German nationals. The investigations there are expected to result in charges of bankruptcy fraud, export violations, and tax evasion against these individuals.

A team of U.S. Customs special agents has recently returned from Lubeck where they reviewed much of the material obtained by the West Germans in the investigation of the Mueller organization. In addition to substantiating the usage of the distribution license system by the Mueller group to obtain significant amounts of

U.S.-origin strategic technology in Europe, documentation and other evidence collected by the Germans reflects that Mueller, Nast, Schroeder, and others were frequently in the Soviet Union installing and servicing U.S.-produced technology that they had diverted there from the United States. Much evidence exists which shows that Mueller funneled this equipment through an intricate labyrinth of shell companies from West to East for years and funded this entire mechanism through a series of Swiss holding companies and bank accounts.

The West German investigation, like that in the United States and in Sweden, is far from complete. We are confident, however, that the spirit of international cooperation, unprecedented in the area of technology transfer investigations, will continue and that it will result in the criminal prosecution of both the companies and individuals involved in these diversions in the United States, West Germany, and Sweden. To date, the enforcement actions initiated by the U.S. Customs Service have resulted in the exposure and dismemberment of the largest technology diversion organization in history. We expect that the investigation will progress and expose further links between Mueller and other major diverters and sever these long established Soviet tentacles.

Senator PROXMIRE. Where is Mr. Mueller now?

Mr. RUDMAN. We believe he's in Eastern Europe right now. I can tell you privately more about it.

Senator PROXMIRE. He's not in West Germany?

Mr. RUDMAN. To the best of our knowledge, he's not, but I get that second and third hand.

Senator PROXMIRE. Can he be extradited?

Mr. RUDMAN. No, sir. The offense is not extraditable.

Senator PROXMIRE. He's a fugitive?

Mr. RUDMAN. Yes. He has been since 1979.

Senator PROXMIRE. And he was indicted for what?

Mr. RUDMAN. For another Export Administration Act violation in California in the mid-1970's.

Senator PROXMIRE. Diverting high technology to the Soviet Union?

Mr. RUDMAN. Yes, sir.

Senator PROXMIRE. That was 1979. They've been on notice since then that this man has been at least indicted.

Mr. RUDMAN. Before that, the original indictment was in 1976 and there was a superseding indictment in 1979.

Senator PROXMIRE. Now, Mr. Rudman, we have closely examined a copy of the January 16, 1984 memorandum of understanding between the Department of Commerce and the Customs Service about enforcement of our export control laws. This agreement really only gives Customs a role in investigating violations of our export control laws outside the United States.

Isn't it fair to say that under this agreement Commerce retains control over general enforcement policy matters and the prelicense and postshipment checks that Commerce fouled up on in the VAX case?

Mr. RUDMAN. Yes, sir.

Senator PROXMIRE. In light of Commerce's poor record on enforcement, does this concern you?

Mr. RUDMAN. I believe that we're on the right track now. Any problems do concern me in the area of any problems between agencies, any confusion does concern me, but I believe that we have very recently in the last month or so made some strides toward better cooperation.

Senator PROXMIRE. But you do give up general enforcement policy matters and prelicense and postshipment checks?

Mr. RUDMAN. Well, we've never had them, sir.

Senator PROXMIRE. That's the problem. They haven't been handled very well by Commerce and my question is: Do you feel at ease that Commerce should continue to have that kind of authority in view of their record?

Mr. RUDMAN. As far as prelicense and postshipment checks, for the most part, yes, if they're routine. If they're ones like the ones here that are connected with an ongoing criminal investigation, I would feel better if the information was shared and we approached it jointly.

Mr. ARCHEY. Well, the MOU, Senator, on postshipment checks requires that anything Commerce gets on a postshipment check that is adverse even if there's not a case ongoing by either organization would be in fact communicated to Customs.

Senator PROXMIRE. How about you, Dr. Bryen?

Dr. BRYEN. We are not involved in those things at all, sir, so it's difficult for me to say.

Senator PROXMIRE. In view of the Commerce record and the fact that they are a trade promoting organization, not an enforcement organization, do you feel that's a fair allocation of responsibilities?

Dr. BRYEN. Well, they have set up under Deputy Assistant Secretary Ted Wu a compliance division which has been pretty effective, generally speaking, much more than in the past. You have to give this thing a chance to work on an interagency basis, unless you feel it's hopeless, at which point——

Senator PROXMIRE. Let me ask you both, Mr. Rudman and Dr. Bryen, reminding you both again that you're under oath, I ask you if there's any truth to the claim made by some that the recent agreements between Commerce and Customs and Commerce and Defense respectively were designed explicitly by the administration so it would have a better basis for arguing against the reforms in the Senate bill during our upcoming conference with the House?

Mr. RUDMAN. I think my parent organization, the Treasury Department, triple insulated me from their thinking on that, so I honestly couldn't answer the question. I have no idea.

Senator PROXMIRE. You can't pierce that triple armor?

Mr. RUDMAN. No, sir. I'm a midlevel bureaucrat in the Customs Service.

Senator PROXMIRE. Dr. Bryen.

Dr. BRYEN. Well, I will be very frank, Senator. We have been seeking to be involved in the West-West licensing process for some time and this resulted in a series of long negotiations and discussions which were held by Assistant Secretary Perle and at some point the Secretary himself with members of Commerce and the White House. To what extent it had an impact on the bill one way or the other, I don't really know. It was going on well before that.

One other point in that connection is that in terms of licensing to CoCom countries, you've got a lot of problems with that House bill which, I think, you're aware of in terms of taking away some of the license processing to the CoCom countries. It is far more risky, it seems to me, than what we're talking about here today. The bottom line is that we won't even have authority to have these licenses in the CoCom countries if the House bill passes. I don't know how we're going to do business then and who we're going to have enforce them.

Senator PROXMIRE. Well, we have a lot more than the material we're discussing today to be concerned about, but here we're concerned with this particular case and with the legislation that's before us at the moment.

LACK OF PRIORITY GIVEN TO EXPORT CONTROL

Mr. Rudman, I think this episode reveals real problems with the lack of priority given to export control duties by personnel attached to our embassies and consulates.

In your judgment, will the administration take any steps to remedy this serious problem?

Mr. RUDMAN. Are you talking about the prelicensing, postshipment checks, Senator?

Senator PROXMIRE. Well, I'm talking about their lack of priority in general, including those.

Mr. RUDMAN. Well, we in Customs have increased our staff of trained criminal investigators, attaches and their assistants, in almost every office and we've added two new offices in the last 2 months. So we have beefed up our overseas representation to insure that at least when Customs is involved, criminal investigators will investigate alleged violations.

Senator PROXMIRE. Mr. Archey, isn't it true that on June 26, 1981, you finally opened an investigation on the information you received in May 1980 about Mr. Mueller's involvement with MRI?

You then closed that investigation on March 10, 1982, solely on the basis of interviews with an MRI official, the firm under investigation?

Mr. ARCHEY. That's correct.

Senator PROXMIRE. Well, doesn't that reveal that Commerce lacks a law enforcement mentality? Would a vigorous enforcement agency rely solely on interviews with the suspect firm?

Mr. ARCHEY. I think the Commerce Department enforcement program in May 1980 and June 1981—I would accept your coloration. I would not accept your coloration now.

Senator PROXMIRE. I'm talking about March 10, 1982.

Mr. ARCHEY. I am saying that up until Ted Wu came aboard in July 1982 I think the Compliance Division which was the predecessor to the Office of Export Enforcement was not a professional law enforcement organization. We think it is today.

Senator PROXMIRE. Now, in fact, Commerce even after receiving more derogatory information in November 1981 about MRI still did nothing but talk to MRI officials until the VAX computer showed up in West Germany on the way to the Soviet Union. Isn't that right?

Mr. ARCHEY. Again, Senator, as I said in both my prepared statement and in response to two previous questions, the November 1982 information provided by the company had one very big out that said that the company, although they didn't want installation, that they had an engineer trained by their own company that could install it and that was very, very much in their own letter saying maybe the way they did it and that's understandable.

Senator PROXMIRE. Thank you, Mr. Chairman. Unfortunately, I have to be on the floor. Thank you. I will have some questions for the record.

[Response to written questions of Senator Proxmire follow:]

RESPONSE TO WRITTEN QUESTIONS OF SENATOR PROXMIRE

FROM

WILLIAM T. ARCHEY, ACTING ASSISTANT SECRETARY FOR TRADE

ADMINISTRATION, DEPARTMENT OF COMMERCE

QUESTION #1

You told us that on November 22, 1982, Commerce received information from a California Corporation that it was suspicious of MRI because it would not allow the company to install equipment purchased from it by MRI. Despite that, Commerce licensed the export of a VAX 11/782 computer system to MRI on December 21, 1982.

Did Commerce ever undertake any investigation of MRI based on the information it received from the California Corporation on November 22, 1982?

If so, describe when that investigation began, its nature, and its results.

Did Commerce continue to license equipment to MRI after December 21, 1982? If so, what, and do you know where the equipment is now?

ANSWER

The Office of Export Enforcement received a letter from a California producer of semiconductor testing equipment on November 29, 1982. While the letter made no allegations against Microelectronic Research Institute (MRI), it did describe some "unusual circumstances" with respect to MRI. Specifically, the California firm informed us that although the price of the equipment purchased by MRI included the cost of installation, MRI had not requested installation services. At the same time, however, the letter cited another factor which lessened the unusualness of this circumstance: that an engineer from MRI had been trained on installation and maintenance of the equipment at the California manufacturer's plant and was generally attested by the firm's Field Service Training Personnel as being the sharpest engineer who had ever been in one of the training classes. Therefore, in the California firm's opinion, it would be possible for this particular engineer to install, set up and maintain by himself the equipment MRI had purchased from the California firm. The firm wished to advise the Department of these unusual circumstances notwithstanding the capabilities of the MRI technician to install the equipment himself.

On December 14, 1982, OEE opened an investigative case based on the letter, and the case was assigned to the San Francisco Field Office of the Office of Export Enforcement. The case was held in inventory by the San Francisco Field Office due to the relatively low-level of information contained in the letter and because, at that time, all the investigators were active in a pressing investigation involving 24-hour surveillance. This investigation lasted from early February 1983 to late March 1983, and was given priority status because significant violations were in the process of being committed, and because the investigation implicated a foreign intelligence service. If action was not taken quickly, the foreign nationals involved would have left U.S. jurisdictional reach.

On March 24, 1983, the MRI case was assigned to a special agent in the San Francisco Field Office. Five days later, he submitted a draft cable message to headquarters to convey to the Cape Town Consulate General (ConGen) a request to conduct a post-shipment check on equipment already exported to MRI. Over the next six months the agent, coordinating with headquarters, requested additional post-shipment checks, telephonically contacted the Cape Town ConGen officer on the matter, collected information from firms which had already exported equipment to MRI, and, early in August 1983, requested the U.S. Embassy in Pretoria to ask the South African government to enter the investigation.

After about mid-June 1983, it became increasingly clear that there was something suspicious involving MRI, primarily because of MRI's refusal or delay in responding to post-shipment check requests by ConGen Cape Town. Meanwhile, however, OEE continued to receive conflicting information on the MRI facility, some of it favorable and some of it unfavorable.

The license application for the VAX 11/782 for MRI to which you refer was originally received in the Office of Export Administration in August 1982, three months before the receipt of the letter from the California firm, and was not referred to OEE for review based on screening procedures in effect at that time.

Finally, in response to the last part of your question, Commerce issued two licenses naming MRI as consignee after December 21, 1982. One was issued for the VAX 11/782, which was subsequently stopped in Hamburg and Stockholm, and another was issued on July 5, 1983, for about $200,000 in software for the previously approved VAX system. This July validated export license was erroneously issued because the OEE case agent and his contact at OEE Washington headquarters failed to place MRI into the suspect name-screening system. This was an unfortunate oversight. The July license, however, was subsequently revoked before any software was exported against it. We would also like to point out that OEE successfully stopped another license application for a photorepeater for MRI valued at $500,000.

QUESTION #2

I understand that on June 2, 1983, another American corporation gave Commerce information that it, too, was suspicious that MRI might be diverting equipment to the Soviets. I further understand that on July 5, 1983, Commerce licensed the export of another VAX computer to MRI.

Is that true? If so, why did Commerce do this?

ANSWER

In early June 1983, OEE headquarters received information from one of the suppliers (under validated export license) to MRI that it believed that MRI may have disposed of its equipment illegally. The supplier had no specific information that the equipment was diverted to the Soviet Bloc, but because MRI had blocked its technicians from installing its equipment at MRI, this supplier believed that the equipment was no longer at MRI and probably had been diverted.

OEE suspected two possible reasons for MRI's refusal to allow installation of the supplier's equipment: one was that the equipment had been diverted outside South Africa. The other reason was the possibility that the equipment was being used illegally by the South African Government, especially the military. Because of South Africa's strong stand against the Soviet Union, we believed that any diversion would most likely have been internal to the South African Government.

On July 5, 1983, a license application was approved for about $200,000 in software for MRI for use on the VAX system MRI had previously acquired. This July 5th application was erroneously approved because the case agent and his contact at OEE Washington headquarters failed to place MRI into the suspect name screening system in the Office of Export Administration. As soon as we discovered this oversight, however, we immediately revoked the July 5th license before any software could be exported against it. Another license application for a photorepeater valued at $500,000 for MRI was stopped by OEE and subsequently rejected by OEA.

QUESTION #3

We understand that on August 5, 1983, Commerce informed our Consulate General in Capetown of its intention to deny MRI further U.S. export privileges because of the risk of diversion to the Soviets.

Why did not Commerce begin efforts at that time to stop diversion to the Soviets of the equipment already shipped to MRI?

ANSWER

On the contrary, Commerce took immediate actions through the only possible channel to stop diversions from MRI to the USSR: OEE requested, through the Cape Town ConGen, the assistance of the South African Government in investigating MRI. We believed that the South African Government, being ardently anti-communist, once aware of our concerns and, hence, our desire for an investigation on MRI, would prevent any diversions from taking place. Because of the obvious sovereignty issue, no U.S. enforcement agency could undertake an investigation on South African soil without the express permission and invitation of the South African Government. While the South African Government did subsequently agree to look into MRI, OEE, unfortunately, had no way of knowing the resources or attention the South Africian Government would contribute to the investigation of MRI, which we later learned were meager.

QUESTION #4

Prior to the Customs action of November 1983, did the United States Government ever request the South African Government's assistance in investigating MRI?

If so, what was the nature of the assistance given and what results did it lead to?

ANSWER

By cable dated August 5, 1983, OEE requested ConGen Cape Town to request the South African Government to investigate MRI. We felt that the South African reaction to the request would give OEE some insight to the question of the possibility of South African Government (SAG) involvement in MRI. A South African investigator was assigned this matter in September 1983. The results were not conclusive because the investigator had some difficulty in establishing facts against MRI and because he broke his leg in the middle of his investigation and was temporarily sidelined.

Another problem was that the SAG investigator never relayed to the ConGen Cape Town the steps he took during his investigation, or any interim findings. Especially important was his failure to relay to ConGen the fact that in September 1983 he learned that Richard Mueller was in South Africa and associated with MRI. None of the results of the South African Government's investigation became known to OEE until February 1984.

In November 1983, U.S. Customs told OEE that it (U.S. Customs) was working with South African authorities on the MRI investigation and that OEE should wait and work through U.S. Customs on this case. U.S. Customs, however, never gave OEE any South African investigative result or report on MRI. In fact, it was South African trade officials who, in February 1984, first gave OEE the results of the SAG investigation of MRI. This came largely as a result of direct communication channels established in December 1983 by Commerce with South African Trade Department officials.

QUESTION #5

Did our government ever receive any cables or other information during the course of its investigation of the VAX diversion containing allegations or suggestions that the South African Government may have benefitted from, or used the equipment shipped to MRI prior to its attempted diversion to the Soviets?

If so, describe the nature and content of such information.

Did you, and do you now, give any credence to such reports? If not, why not?

ANSWER

On June 27, 1983, OEE received a cable from Cape Town reporting on an interview between MRI's managing director (Dr. Harrison) and the ConGen officer overseeing the matter. This cable reported that the managing director believed that MRI was a front for the South African military, and that the equipment obtained by MRI from the U.S. was being used for military-related research by the South African government. We had no credible information then, nor do we now, that would substantiate Harrison's statement.

As I stated in my answer to question 4, on August 5, 1983, OEE requested that the South African Government be approached by ConGen Cape Town, to request their assistance in our investigation of MRI. We believed their reaction to our request would give us some indication of their involvement with MRI.

We received a second cable from the commercial officer at Cape Town ConGen after the seizure of the VAX 11-782 in November 1983 raising the possibility of South African Government interest in MRI, but the information was presented as opinion by the commercial officer, and was never verified. A subsequent cable from ConGen referred to the earlier cable about possible SAG involvement in MRI as supposition rather than fact.

There is no doubt in our minds that all of the available evidence now points to MRI diversions solely to communist-dominated countries. No evidence exists to implicate the South African Government at this time.

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE
WASHINGTON, D.C. 20301

INTERNATIONAL
SECURITY POLICY

1 MAY 1984

In reply refer to
I-08257/84

Honorable Jake Garn
Chairman
Senate Committee on Banking,
Housing and Urban Development
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for your recent letter, in which you passed along a question Senator Proxmire wanted answered surrounding the recent VAX diversion case.

QUESTION: Did our government ever receive any cables or other information during the course of its invescigation of that VAX diversion containing allegations or suggestions that the South African Government may have benefitted from, or used the equipment shipped to MRI prior to its attempted diversion to the Soviets? If so, describe the nature and content of such information. Did you, and do you now, give any credence to such reports? If not, why not?

ANSWER: From the cable traffic I have reviewed, I came across no information to suggest that the South African Government may have benefitted from, or used the equipment shipped to MRI prior to its attempted diversion to the USSR. I offer this caveat, however, to my comment. The Defense Department was not a recipient of any cables surrounding the entire licensing process with MRI. From cables we have reviewed since the episode became the subject of an investigation, I believe the South African Government knew nothing of the transaction. Because MRI was set up to divert goods to the USSR, it is unlikely the company would have notified the South African government about the equipment. In addition, the United States does not require an exporter in South Africa to seek an import certificate (IC) to receive controlled commodities in that country. Consequently, MRI never would have had to notify the South African government of the transaction. At present, the United States requires IC's only to COCOM and a few other countries, but not South Africa.

I trust this response will be helpful.

Sincerely,

Dr. Stephen D. Bryen
Deputy Assistant Secretary
International Economic, Trade and Security Policy

The CHAIRMAN. Gentlemen, just for a moment let me confer with staff so that I don't start asking you some questions that Senator Proxmire has already asked.

Mr. Archey and Mr. Rudman as well, did our Government ever receive any information during the course of this investigation that the South African Government may have benefited from the equipment shipped to MRI prior to its diversion to the Soviets?

Mr. ARCHEY. To my knowledge, we've never received any information of that sort.

Mr. RUDMAN. Same answer, sir.

The CHAIRMAN. That was simply just a rumor. The reason I asked the question is because it was my understanding that it was just a rumor. There was no involvement of the South African Government and I wanted to have that cleared up for the record. There was no substantive information at all that that was the case.

Mr. Rudman, will the Customs Service be able to enforce OEE by itself without any Commerce enforcement operation?

Mr. RUDMAN. Would it, sir?

The CHAIRMAN. Yes.

Mr. RUDMAN. Yes, we would. I would just point out that we enforce and have always enforced exclusively the statutes of the Office of Munitions Control, a companion of the Export Control Act.

The CHAIRMAN. Mr. Archey, could the Commerce Department adequately enforce the OEE without Customs?

Mr. ARCHEY. No, sir.

The CHAIRMAN. That's what I thought.

Mr. ARCHEY. And I don't agree with the other side of it. If you have Customs only having enforcement program, you're going to see massive delays in licenses; you're not going to have prelicense and postshipment checks that are now being done correctly. You're not going to have a licensing screen done in a timely manner. You're not going to have the benefit of the ability of the interface between licensing technical people and enforcement people and I think you are going to go against what you are in fact for, Senator. I think if the licensing function does not have an enforcement arm to it, I think it's going to be to the detriment of the business community and to the detriment of the licensing.

The CHAIRMAN. All I can say is Commerce has virtually ignored the enforcement section over the years. I'm not talking about just recently, but over the years it virtually ignored it.

Mr. ARCHEY. Nobody would disagree with that. The other point I'm trying to make in terms of context because although Bill and I sometimes get into disagreements, I spent 3 years with Customs so I'm extraordinarily proud of that association. I think it's an extraordinary organization. And I also think that back in the 1970–80 era the Customs Service wasn't paying much attention to exports up until late 1981 when through Steve Bryen and Richard Perle there was a massive transfusion or transference of funds, but it was not a priority—dope, fraud, a lot of other things, but not export controls, and all I'm saying, Senator, is I think it's only fair to say in the context of—I will not deny—nobody can deny that the Commerce enforcement program was not professional and it was

not aggressive, but there was no such thing anywhere in the Gov ernment in terms of an aggressive enforcement program.

CUSTOMS IS A LAW ENFORCEMENT ARM OF GOVERNMENT

The CHAIRMAN. I don't disagree with what you've said about Customs involvement prior to 1980 or 1981. The point I make is that Customs is a law enforcement agency. It always has been. It has been set up and trained for that specific purpose and once that direction was given to them they performed rather well under some difficult circumstances. The enforcement division of Commerce never has been a law enforcement agency. Commerce is not a police agency. It is not an investigative agency and I think that tells the story. Customs is more effective. You've served as both. Commerce is to support commerce. Customs is to catch people doing wrong things.

Is that your experience in working for both of them?

Mr. ARCHEY. Not to that point because I think where the Commerce——

The CHAIRMAN. You're missing my point. I understand what you said about Customs not doing it before, but Customs is a law enforcement agency specifically trained for that purpose with expertise and background and as soon as they did get into enforcement of trade export administration and so on, they have done a good job under difficult circumstances.

Mr. ARCHEY. I think Customs has done a good job. I agree.

The CHAIRMAN. So all the evidence indicates to me that it is possible for Customs to do the job themselves and that the interface couldn't be worse than your internal interface with your own enforcement division over the years. Again, when I say your—I'm not personally criticizing anyone. I am criticizing a system that has not worked and yet there is a fight to preserve that system with minor improvements. Regardless of how much sincerity there is to improve it, I don't know how you can solve that problem internally at Commerce and solve that interface problem internally. It seems to me you can work with Customs and give them the enforcement ability and still work with them on the licensing end of it.

Mr. ARCHEY. I think we will do that anyway, but I am saying that I think the internal arrangement and working arrangement between licensing and enforcement in the Department right now is excellent. I think that we're showing that. I think we are showing that in terms of just having established an organizational structure that's looking at historical data from the technical point of view, looking at commodity profiles, looking at profiles of one issue that I think we are starting to realize now—original equipment manufacturers [OEM], particularly of computers, of people who receive U.S. computers. We're doing profiles on which OEM's really look right and which don't look right and we're going to share that also with the business community in order to guide their own determinations on who they sell to.

I am saying that I think an effective law enforcement program requires both agencies. I genuinely believe prior to the President's decision that the roles were complementary. I don't see them as a zero sum game. In late 1981 when I was Acting Commissioner of

Customs I had a personal involvement in this because I had my job on the line in April 1981 when I authorized the seizure of the Aeroflot plane at Dulles. We didn't find anything. I was told pretty much you're in trouble, but that was a decision that had to be made. That decision was really the first shot fired in the administration—any administration that highlighted the Export Administration Act and in late 1981 some of Bill's bosses came to me and said, "Let's take over the program." I was Acting Commissioner of Customs at the time. I said I thought Commerce had a legitimate enforcement role because of the licensing function. I said it back then and I'm saying it still now and I have even more reason to believe it now.

The CHAIRMAN. In response to your comment about being in trouble, you wouldn't be in trouble with one of us. Suppose we stopped Aeroflot or someone else and there was nothing on them over, and over, and over again and we caught them once in a while. It's worth it.

Mr. ARCHEY. That's right.

The CHAIRMAN. Anybody who's been in the other countries and knows how you're checked at the border going in and out, knows we're so loose it is utterly ridiculous. If you ever do that again and you want somebody to back you, we will. So they were inconvenienced for a few hours—big deal.

Mr. ARCHEY. Well, I would say one thing about the other aspect of the Customs role in this, although Exodus receives a lot of complaints. We're seeing something, for example, the whole shift in licensing review and enforcement review is going West-West cases. We are having a decline in the number of cases going West-East in the last few years. That has been more than compensated for. In the month of February, Senator, we had license applications annualized at the rate of 140,000. That's from 95,000 in 1983. Part of that increase has come from the fact that the Exodus program is there and most of the increase in applications isn't because the bad guys are coming in the system but because people didn't know they required a license. That's one. No. 2, I think now if somebody truly wants to divert without going through the license process and seeks to corrupt the license process by lying or whatever, that what's happened is it's going to make it more difficult. I think what happened with the Customs aspect of the program, it's made people a lot more wary that in fact even given the point you make about maybe we still have a sieve, it's a hell of a lot tighter now than it was in 1981 when nobody was checking on it.

NEED TO HAVE IMPROVEMENTS SET INTO LAW

The CHAIRMAN. That gets back to another question. Let me assume that the MOU works well, improvement continues and everything you say works out to be true. You're right and I'm wrong and suddenly we get a change in administration to one that has a different attitude. If these things we're doing are so good, why can't we put them in statute? I know you're going to say flexibility. Why? If it works, and works well, why not put it in law so that some future administration——

Mr. ARCHEY. It may be the President may want to have some other entity within the Government be involved with enforcement. It may be again this issue of flexibility, but it may be other options besides what we've thought about now.

The CHAIRMAN. Look at some of the attitudes in the House right now. You've got a wonderful bill over there.

Mr. ARCHEY. Well, Steve and I were just discussing the fact that Commerce shares a great concern about the fact that we are talking about this one case of South Africa. We're talking about the fact that we may not have licenses going to CoCom countries. That is of considerable concern of our Department and to Steve's. We think, for example, if you don't have that license, one of the things we're starting to see and Bill is starting to see, we're making more and more cases on the basis of the fact that more companies have to come into the licensing process and they don't want to be caught—when they go into the licensing process they have to if they're going to divert and engage in some type of deception. Well, we need that audit trail and the fact still remains—and I don't think anybody can dispute that—most diversions are still occuring out of Western Europe and we think it's very important to have that trail.

The CHAIRMAN. I've made several statements on the floor. I'm a little bit tired of our allies continuing to bellyache about extraterritoriality and so on when most of the diversions are occurring through Western Europe. They have been involved in a lobbying campaign that I think is unprecedented. Ambassadors of other countries have been involved in direct lobbying of this body. They could go through the normal State Department channels and we would be informed. I'm sure that the British wouldn't like our Ambassador to be directly lobbying Members of Parliament on particular issues. But I'm just a little bit tired of hearing their bellyaching when they don't do their own fair share of defending their own territory. They haven't kept their promises of going to at least 3 percent real growth in their own defense budget, and 40 years after the end of World War II to still allow us to maintain a very large standing army in Europe and provide the umbrella of their defense. All the while, they want to continue business as usual and sell everything they can of their own products and ours to the Soviet Union without worrying about it.

I'm just getting very tired of that kind of attitude so I see nothing wrong with import controls either. Look at the Japanese, they can jump into the Soviet-European oil pipeline project and claim that is not high-tech sales. Then we hear the old excuse that what we don't sell, somebody else will. Unfortunately, it is too true. The Japanese have less than 1 percent of their gross national product in defense and an incredible trade deficit. My comment has been and continues to be that if they don't want to cooperate on the West-West trade issue, why don't they try to sell some Toyotas and Datsuns in Moscow and see how well they can do. They come over and take more than 20 percent of our car market, and we've had massive unemployment along with that. I don't think they could sell too many cars in Moscow.

Again, I guess I'm stepping out of role. I'm normally for free trade as long as it's fair and all of that, but I'm really getting very

sick and tired of our allies' attitude on this and as well as their continuing attempts to defeat the Senate version of the Export Administration Act. If they want to play that kind of game, then some of us will start talking again about amendments like Senator Stevens and bring some of the people home from Europe, which I don't really want to do, but somehow we've got to knock some heads over there. Maybe they still think we're a colony. I don't know. They certainly have a superior attitude. It becomes easier for me all the time to understand why they've been involved in so many wars. They never learn. Over and over again they have defeated the enemy and now we're back to Neville Chamberlain again. Over and over again they suddenly wonder why they're in the war and ask us to come and bail them out.

Now we're getting off on another subject but it certainly illustrates the point that West-West trade is the biggest part of the problem no matter how much they protest, they have not been doing their job and CoCom has not been doing the job that should be done. It's a tragedy when you think what the stakes are. Forget the dollars we're losing in the defense budget as a result of this. We're talking about the future makeup of this world, the struggle between capitalism and communism, and capitalism is so willing to sell anything that they don't worry about the end result. Lenin talked about us selling a rope by which we would hang ourselves. I guess he didn't anticipate that we'd loan them the money to buy the rope.

Gentlemen, thank you very much for your patience. It's a difficult problem. You performed very well and I think, Mr. Archey, you have been the best defender that Commerce has ever sent before this committee. You still haven't convinced me, but you've been the best. Thank you very much.

The committee is adjourned.

[Whereas, at 12:25 p.m., the hearing was adjourned.]

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